

Tax optimization of your investments in Central and Eastern Europe: focus on Poland, Hungary and the former Yugoslavia region

François Hellio, László Trócsányi, György Hevér, Arkadiusz Michaliszyn, Tamara Stručić, Eszter Kálmán, Tamás Fehér

Poland – selected tax aspects

Arkadiusz Michaliszyn
partner, CMS Cameron McKenna LLP, Poland
arkadiusz.michaliszyn@cms-cmck.com

Poland

- Area: 313,000 km²
- Population: 38.1 M
- Capital: Warsaw (2.5 M people)
- Unemployment: 12% - 13%
- Average net salary (median): approx. 500 Euro
- Increase of GDP: 2011 - 4%, estimation for 2012 between 1% - 4%
- Public debt to GDP: 55%

SEZ – basic information

- Certain areas (14), existing for a specified period of time (till 2020), in which enterprises can perform their business activities under privileged conditions, after meeting certain requirements
- Form of public aid granted in order to enhance new investments and create new workplaces in specified regions in Poland

SEZ – forms of public aid

- Public aid available in SEZ could be provided in a form of:
 - corporate income tax relief
 - real estate tax relief
 - cash grants

SEZ – forms of public aid (cont.)

- Two elements are taken into account to calculate the maximal amount of the public aid:
 - the value of the eligible costs of the new investment (such as property, assets and intangibles) or labour costs (2-years labour costs)

multiplied by

- public aid intensity rate

SEZ – forms of public aid (cont.)

- Public aid intensity rate depends on the localisation of SEZ and size of the investor. It ranges between:
 - 30% - 50% for large enterprises
 - 40% - 60% for mid-sized enterprises
 - 50% - 70% for small-sized enterprises

SEZ – corporate income tax relief

- The taxable profit generated by an enterprise within SEZ is exempt from CIT up to the value of the public aid

SEZ – corporate income tax relief (cont.)

- the business activity, on which profit is earned, is specified in the permit given to the enterprise by the entity managing the SEZ
- the enterprise's business activity is conducted within the SEZ; and
- the enterprise, for at least 5 years:
 - implements a set number of new investment projects made within the SEZ or
 - creates a set number of new jobs within the SEZ

SEZ – real estate tax relief

- Local authorities can exempt the enterprise from real estate tax

SEZ – cash grants

- Cash grants are available within the Innovative Economy Operational Programme and they could cover:
 - investment in new technological solutions;
 - innovative investment into a manufacturing sector;
 - shared service, IT and R&D centres;
 - industrial design solutions

Financing a Polish company

- Equity financing:
 - share capital: 0.5% capital tax, no interest, distribution through dividends and repayment of the share capital
 - premium: no capital tax, no interest, distribution through dividends and repayment of the share capital
 - additional payments: 0.5% capital tax, no interest, distribution through return of the additional payments

Financing a Polish company (cont.)

- Debt financing:
 - shareholder loan: no capital tax, requirement to charge interest, thin capitalisation, distribution through interest and repayment of principal of the loan
 - non-shareholders loan: 2% capital tax (in practice not applicable), requirement to charge interest, no thin capitalisation, distribution through interest and repayment of principal of the loan

Former Yugoslavia region – selected interpretations of local tax authorities based on tax inspections

Tamara Stručić
lawyer, CMS Reich-Rohrwig Hainz, Croatia
Tamara.strucic@cms-rrh.com

Selected issues across the region

- Slovenia: transfer pricing and customs
- Croatia: input VAT refund
- Montenegro: withholding tax on consulting services
- Serbia: factoring and VAT
- Bosnia: loss-bearing transactions between related parties

Slovenia: transfer pricing and customs

- Case:
 - Import at transfer prices, using the resale method
 - Transfer price adjustments based on audited P&L
 - Accepted practice for 5 years
 - Year 6: price adjustment no longer accepted, although accepted for CPT; documentation deemed insufficient
- Outcome: 180 cases won before the administrative court; return to first instance, order to provide evidence why transfer price equals customs base
- Conclusion: documentation requirements are stricter than under transfer pricing for tax purposes

Croatia: input VAT refund

- Input VAT refund denied in case services are not sufficiently specified
- Case: law firm having received invoices from „sub-lawyers“, including detailed service specifications
- Tax authorities wanted to see „proof of work“, ie. legal and tax opinions sent to clients
- Although Croatian BAR association intervened, this practice can be seen also in various other cases
- Conclusion: extremely strict requirements towards service specification

Montenegro: withholding tax on consulting services

- Case: Foreign entity (UK resident) rendered consulting services to MN entity
- MN tax law prescribes WHT on such services
- DTT does not allow MN to levy WHT
- Tax authorities nevertheless issued an official opinion to the taxpayer that WHT is due
- After 3 months of consultation with the MN authorities, they were convinced that WHT is not due

Serbia: factoring and VAT

- Factoring as sale of receivables is considered to be a VAT-able service
- The factor purchased a receivable with a discount, constituting the factoring service
- Serbian Tax Authorities ruled that if the initial receivable was not VAT-able (such as a banking receivable), the factoring service is also not VAT-able
- Reason: following GFKL-ruling

Bosnia: loss-bearing transactions between related parties

- Bosnia is generally divided into three jurisdictions: (i) Federation of Bosnia and Herzegovina; (ii) Republika Srpska and (iii) District Brcko
- Due to considerable „tax optimization“ in the past between these jurisdictions, losses between related parties are only recognised under certain circumstances:
 - Republika Srpska: tax losses on transfer of assets between related parties → not recognised
 - Federation: tax losses from business between related parties cannot be carried forward

Hungary – the new Real Estate Investment Trust system and the capital gains exemption regimes

Eszter Kálmán

senior associate, CMS Cameron McKenna LLP, Hungary

eszter.kalman@cms-cmck.com

Tamás Fehér

associate, CMS Cameron McKenna LLP, Hungary

tamas.feher@cms-cmck.com

The new Hungarian Real Estate Investment Trust system

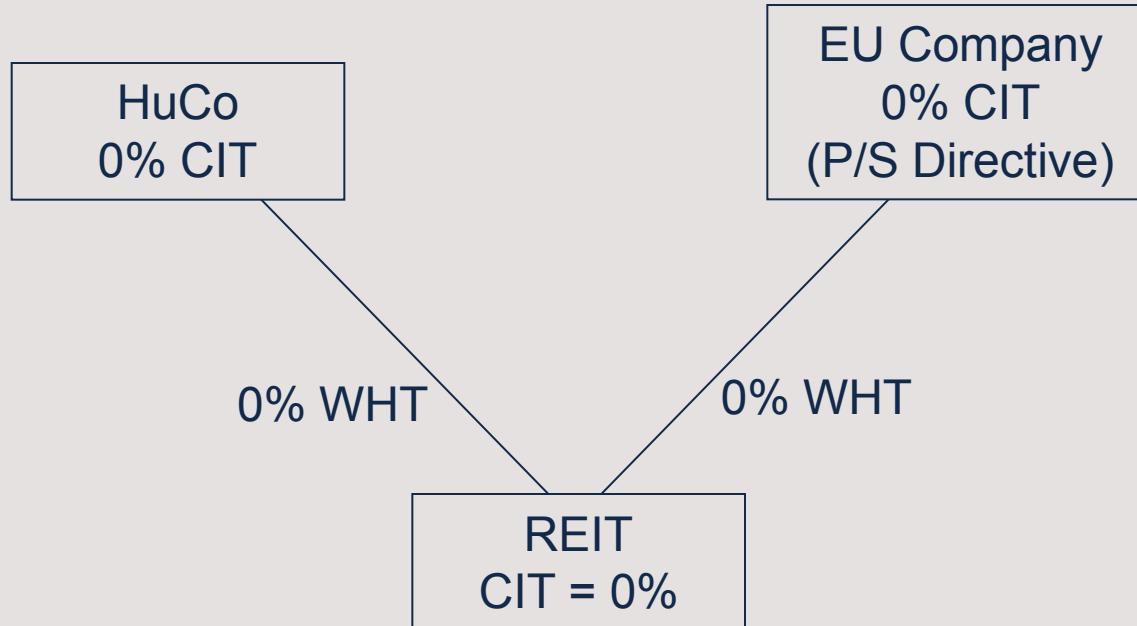
- REITs in general
 - Exemption from corporate income tax and local taxes
 - Requirement of listing of at least part of the shares
 - Activities restricted to those related to real estate
 - Mandatory distribution of income
 - Conversion charge upon entry into the REIT system

The new Hungarian Real Estate Investment Trust system (cont.)

- The benefits provided by the Hungarian REIT system
 - Exemption from CIT (except for revenues from non-qualifying related parties)
 - Exemption from local business tax
 - Preferential rate (2% vs. general 4%) of transfer tax for acquisition of property

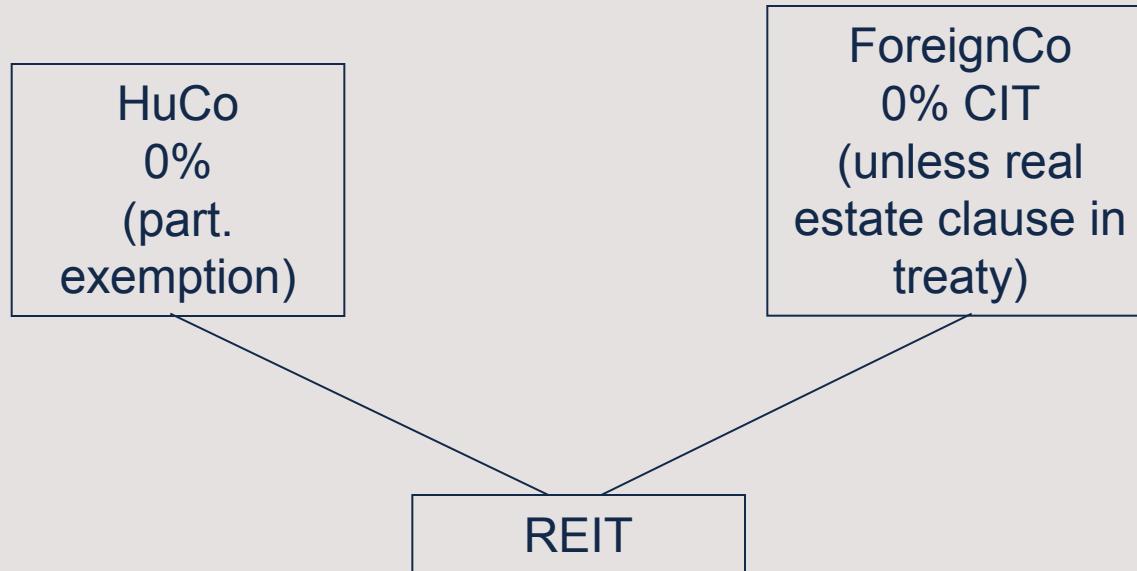
The new Hungarian Real Estate Investment Trust system (cont.)

- Dividends paid by REIT



The new Hungarian Real Estate Investment Trust system (cont.)

- Taxation of capital gains



The new Hungarian Real Estate Investment Trust system (cont.)

- Legal requirements
 - Ownership structure
 - at least 25% of the shares shall be traded on a stock exchange
 - at least 25% of the shares shall be held by small investors (holding less than 5% each)
 - no more than 10% of the shares and the votes to be owned by insurance companies and credit institutions

The new Hungarian Real Estate Investment Trust system (cont.)

- Legal requirements (cont.)
 - Activities and investment
 - Activities limited to: real estate sale, leasing, operation, property management and asset management activities
 - The value of real estate portfolio held directly or indirectly is at least 70% of balance sheet total
 - Scope of other assets is limited (bank deposits, government bonds, listed securities, participations in real estate companies, etc.)
 - Real estate portfolio may contain properties located in Hungary as well as outside Hungary
 - No more than 20% of balance sheet total invested in a particular property

The new Hungarian Real Estate Investment Trust system (cont.)

- Legal requirements (cont.)
 - Capital and dividend policy
 - minimum capital: HUF 10 billion (approx EUR 32 million)
 - at least 90% of distributable profits must be paid out as dividends within 15 days of the approval of its annual report
 - debt financing may not exceed 65% of the value of the real estate portfolio

Capital gains exemption regimes

- Affecting:
 - Capital gains from the sale of participations
 - Capital gains from the sale of IPs
- Common features:
 - Full exemption from corporate income tax (no other taxes apply)
 - Notification requirement (missed 60-day deadline not remediable)
 - 1-year statutory holding period
 - Capital losses non-deductible
 - Available to relocating entities

Availability to relocating entities

- Foreign-registered entities may relocate their place of effective management to Hungary
- Usual result: Hungarian tax residence (if DTT is available)
- 60-day notification deadline opens up with respect to existing IPs and participations
- 1-year holding period applies from date of purchase (not from date of relocation)
- Benefits may be limited by exit tax rules in country of emigration

Special features: IPs

- Coupled with other benefits:
 - 5% effective tax rate on royalty income
 - roll-over relief available to non-notified IPs
 - Capital gains remain tax free if used within the 3 following years to buy new IPs
 - New IPs may then be notified, ultimately achieving full tax exemption

Special features: participations

- Initially, at least 30% must be held and notified
- Thereafter, any increase in percentage or value may also be notified

Thank you!

Do not hesitate to contact us for questions or queries!