

The TAX Issue

From Russia with love

Kremlin says no to
new taxes and hikes

– *Pepeliaev's*
Anton Nikiforov

Brazil:

In-house counsel tackle the
world's most complex tax
system

Looking at *Austria* from
the outside in

Interview with KPMG's
Michael Glover

Is the *Hungarian*
government
exchanging your
tax info?

Romania:

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Editor's note

Throughout history, the word “tax” has always had a negative connotation. Wars have been fought over taxes and famous people have gone to prison. Today in the aftermath of the 2009 financial crisis, tax is again a major issue for both individuals and companies as governments have gone to extraordinary lengths to fill now depleted coffers.

So Tax is an important issue and it's one we wanted to get our arms around. What we have learned from interviewing the people in the trenches is that being a tax advisor these days is akin to being a bodyguard, if not a superhero.

The modern day tax lawyer is key to business operations and an instrumental figure when it comes to business performance. The bottom line is, they save your bottom line.

What was fascinating about this issue is the diversity of the people we talked to and how they approached their work similarly, but differently depending on what country they are in and the tax codes they had to navigate.

In Brazil, for example, having the right tax advisor could mean the difference of millions or even billions of dollars. Described by the World Bank as the most complicated tax code in the world, the byzantine system is a mix of an archaic structure combined

with a new electronic filing system that results in every filing being looked at under a microscope. An extremely aggressive tax authority and audit structure also means that every move a business makes is heavily scrutinized. Many businesses are now fighting in court to save billions of dollars, which is a giant red flag for foreign investors.

In Russia meanwhile, the government has taken a different path decided not to introduce new taxes or to raise the rates of existing taxes. Instead, the priority has been to abolish ineffective tax benefits and make tax collection more efficient.

And In Romania, economists and lawyers work together to advise corporate clients on a range of issues related to M&A, corporate structuring and even litigation.

Understanding tax law is a science and a rigorous discipline. These people actually make tax seem cool or dare we say, even sexy.

Kevin Livingston
Content Manager –
Emerging Europe and Latin America

Legalis

Big 4 continue to add law firm to their multidisciplinary offerings

Interview: Alexandru Reff, Managing Partner of Reff & Associates – Deloitte Legal – Romania



Alexandru Reff and his firm Reff & Associates have been synonymous with the bigger name Deloitte since the 1990s in Reff's home country of Romania. The correspondent law firm of Deloitte Romania is integrated with the Deloitte multi-disciplinary advisory practice and affiliated to a network of law firms and legal departments working with Deloitte all over the world. The professionals working with Reff & Associates have significant experience in high-level transactions, in which complex matters are addressed from cross-border and multi-disciplinary perspective. GC Grapevine caught up with Alexandru Reff to ask about this success.

GCG: How did the relationship with Deloitte begin?

Reff: I started at Deloitte as an intern in 1997, when I was in my senior year at law school, then joined on a full-time basis in 1998, after graduation. As in most other cases, it was hardly a strategic decision but rather by chance to get involved with this professional environment. For a couple of years I was one of only two attorneys in the Tax practice of Deloitte and gradually got involved with increasingly complex legal work. We started hiring other lawyers and by 2002 we had a small team focusing exclusively on the legal business and doing so successfully. The next year we assisted Citibank on a \$40 million leveraged management buyout, one of the very few of its size and complexity to date. Today, Reff & Associates has more than 40 lawyers and is one of the most respected legal practices within the global legal network of Deloitte.

GCG: Your relationship with Deloitte has spanned over 15 years. Can you single out any one particular career milestone you'd like to share with the GCG, that perhaps is yet unknown about Alex Reff?

Reff: One of the best things about an environment such as ours is that you may have a 15-year career (or probably 40-year career for that matter) with the firm without getting bored or reaching a ceiling. You may constantly change your focus or complement it with different other initiatives, you may change practice areas, countries, industries and management roles such that you may have a new challenge every few years. I was a tax lawyer for a few years, which gave me an invaluable understanding of this essential part of every business and transaction. I worked abroad, having spent one year in the Paris legal practice. I had various management responsibilities, having led the Tax & Legal practice of Deloitte not only in

Romania but, for a couple of years, also in Bulgaria, Albania and Kosovo and I coordinated the Deloitte legal practices across Central Europe for about four years. I am now leading talent-related initiatives for the global legal network and coordinate an initiative to build a real estate practice group across our various functions and service lines in Romania.

GCG: Can you describe the association between Reff & Associates and Deloitte? How does one segregate the legal arm from tax within a Big 4 firm or do you at all?

Reff: Reff & Associates is a law firm that is part of Deloitte network working closely with the various service lines of Deloitte with the aim to provide clients comprehensive, superior-quality assistance in executing transactions and growing their businesses. The legal firm is operationally and functionally fully integrated into Deloitte. While Deloitte and the other Big 4 firm have traditionally been associated with accounting, tax and financial services, today these firms have developed into complex, virtually all-encompassing multidisciplinary practices and law is a critical element of the service offering. There are obvious synergies between legal services and most other types of expertise at Deloitte, but indeed law is

closest to tax, which in itself requires a combination of law and accounting skills. At Deloitte, the tax and the legal practices are very closely integrated, not just from an organizational perspective but also in terms of shared identify between professionals, which is very powerful.

GCG: The trend we are seeing among the Big 4 firms is clearly to strengthen the legal arms across the board. Do you agree with this view and where do you see future growth potential?

Reff: It clearly makes sense for Deloitte and other Big 4 to develop stronger legal arms as they are responding to an expectation of their clients and are increasing their market penetration. There are many reasons why this is sensible, but also brings some challenges, particularly given that law is a profession with a strong identity and culture. I have no doubt in my mind that both the Romanian legal market as a whole and the Big 4 share of this market will grow. The market for legal services globally is estimated to be \$1 trillion per year. That is much larger than the combined markets for all the other professional services offered by the Big 4. Any additional small bit of this huge market, which a firm like Deloitte may acquire, will translate into significant revenues and opportunities to introduce other services in a synergistic manner.

GCG: What do you see as the prime sector focus in the first half of next year for the Big 4 in Romania and why? We are also seeing some consolidation among law firms across emerging markets, meaning more mergers and tie-ups. Any com-

ments on what influence this may have on the Big 4 legal arms?

Reff: I believe the global trend towards consolidation will continue as globalization forces law firms to operate with much more of a local presence than most of them traditionally have. As opposed to the Big 4 firms, there are relatively few law firms, even among the largest ones, which have a comprehensive global presence. In addition, life is getting tougher for lawyers and some firms may not do as well as others under the pressure of the changing business environment. For the Big 4 this means fiercer competition particularly as some firms are developing additional capabilities (primarily tax) and are increasing their global presence, which are currently two of our competitive advantages. In Romania, there may come a time when smaller or even mid-sized firms may have to merge in order to play at a certain level where one needs critical mass to ensure depth of specialization, brand recognition, economies of scale, etc. I am not convinced this time is now and I do not believe that the market will ever be completely dominated by large players – this is a very dynamic business in which the personal skills and relationships are so important that new firms will always emerge as spin-offs of larger ones and entrepreneurially-managed practices will always do well despite their size.

GCG: What has been the secret of your success in terms of human capital decisions and the constant, steady growth of your business?

Reff: In this business, probably like in any other, success is a combination of many ingredients, including

good fortune, which we had plenty of. I would give us some credit for having had a vision and for having pursued it with discipline and hard work over a good number of years. However, if there is one key success factor for us it has clearly been the ability to assemble a team of outstanding professionals with a very strong commitment to the project. We have always been good at attracting talented young lawyers (this year had two of our first year associates in the top three performers at the bar exam) and growing them quickly into great lawyers. We are not the largest, most spoken about firm, yet we enjoy wide recognition for the atmosphere in the team, for how we work and interact with each other, for the learning opportunities, for how people identify themselves with the project. Our success is largely about the long-term, personal engagement of our team. ■

About Reff & Associates

Reff & Associates is a member of Deloitte Legal, the international network of legal practices and integrated with the Deloitte multi-disciplinary advisory practice.

*Areas of focus:
Mergers & Acquisitions
Corporate & Commercial
Capital Markets
Banking & Finance
Real Estate
Insolvency*

*Professionals:
Partners: 2
Lawyers: 42*

Location: Bucharest

Handling tax in Hungary: Don't get buried in paperwork

Interview with Michael Glover, Senior Partner and Head of Tax at KPMG

British-born Michael Glover is a veteran of three large accounting firms, including two that no longer exist. Since 1998, Glover has been with KPMG and for the past 10 years he has led the firm's tax division, a job that has him overseeing more than 200 people. We sat down with Glover to get his thoughts on managing client expectations and doing business in Hungary.



GCG: Please tell us a bit about your background. How did you come to be the senior tax partner at KPMG?

Glover: Having started my career in 1984, I qualified as a chartered accountant in 1987 and became specialized in taxation from 1988 when I left a small accounting firm to join Arthur Andersen's London office. In 1991 I joined Coopers & Lybrand and moved to their Kiev office in 1998. A few months later I moved on to KPMG, still in Kiev, before coming to Budapest at the end of 2000. I became head of the tax function in 2003 when our team was around 35 strong. Since then our tax business revenues have grown nearly eight times over and I am responsible for more than 200 people.

GCG: Please give us an overview of your position and day-to-day work.

Glover: We have three business lines within the tax function. Within those business lines we have specialist groups dealing with VAT, corporate income tax, personal taxes, M&A tax, Transfer Pricing, Financial Services and Corporate Intel-

ligence. My main role consists of delivering growth each year by balancing our resources and investing in areas that we believe will bring profitable growth to the business. Over the years, we have capitalized on new business opportunities by investing in the VAT specialism prior to Hungary's EU accession, building a transfer pricing team when the government initially introduced new requirements in that area and most recently European VAT compliance. I still retain client responsibilities, but I also spend a large part of my time managing the business, interviewing potential new hires and making sure we have a positive working atmosphere based on our core values of respecting each individual, leading by example, working together and acting with integrity.

GCG: From a tax perspective, what are the major challenges companies have to face doing business in Hungary? The EU?

Glover: The main challenges for companies in Hungary are keeping up to date with the latest tax authorities and ministerial interpretations and ensuring paperwork will stand

up to scrutiny during tax authority audits. Hungary is predominantly a form over substance jurisdiction, which means that paperwork often assumes an importance in excess of its true value. From a structural tax perspective, leaving aside the specifically focused sector taxes, the biggest distorting factor is the high level of social security charges. The largest companies bear this high cost, but the small and medium-sized businesses tend to minimize their compliance in this area, which leads to a greater than necessary (or healthy) black economy.

Concerning the EU, VAT fraud remains a significant challenge and we expect continued focus from the legislators in this area. The oxymoronic "tax morality" debate continues to be played out noisily in the media and by governments across Europe. A cynic might suggest that this is an attempt to shift focus away from the inefficiency of governments and on to a target group, which cannot vote.

GCG: Has the tax code significantly changed in Hungary in the past 10 years since the country joined the EU?

Glover: The tax code changes every year, but this is not necessarily linked to being an EU member. The most significant tax changes directly related to EU membership required an alignment of the VAT system with the 6th directive and associated jurisprudence, plus a tightening of the subsidy and tax allowance regime for significant investments into Hungary.

GCG: What is the best advice you would give to a foreign company looking to establish operations in Hungary?

Glover: Take advice from someone who understands the tax and business environment. It is worth paying for quality.

GCG: Would you describe Hungary as being generous with tax subsidies as a way to lure more foreign investment?

Glover: Like all EU members, Hungary must abide by the strict rules on state aid. Hungary is as generous as it is able, within the EU legal framework. I do believe the government is keen to attract foreign investment, which will bring more jobs, especially in the manufacturing sector.

GCG: What types of questions do you most frequently receive from your clients?

Glover: During the past two or three years, the tax authorities became more aggressive in their pursuit of revenue and so our business has been more focused on helping our clients to reduce tax assessments, penalties and interest. VAT and transfer pricing are often to the fore

in tax investigations. In addition, due to reducing tax advisory budgets, our clients have less money to spend and so we have looked closely at benefit sharing opportunities for our clients, especially in obtaining refunds of overpaid taxes.

GCG: What are the biggest challenges you face in your position?

Glover: Managing expectations is always a challenge, especially where different parts of the business are at varying stages of development. Fast growth areas and high performing individuals need a different approach than those parts of the business that are most impacted by the depressed economic conditions, both in Hungary and elsewhere. Clear and consistent communication becomes increasingly important and it is vital that decisions taken are objective and their rationale can be explained. People need to trust that their boss will act in a fair way and that there is a justification for their actions, even if that may not be immediately obvious. In addition, it remains challenging to keep growing the business each year and ensuring that the staff and management are aligned with the growth objectives.

GCG: Do you see any major changes coming in the New Year related to tax?

Glover: One of the great things about tax is that it is bound to change every year. Opportunities exist where there is change. I don't believe there will be a significant change to the structure of the tax system, but there are always areas to be tightened up, actual or perceived problems to be dealt with,

1984: Started career

1988: Left small accounting firm to join Arthur Andersen in London

1991: Joined Coopers & Lybrand

1998: Moved to Kiev office. Joined KPMG soon after

2000: Moved to Budapest

2003: Took over as head of tax at KPMG

and perhaps some concessions to be granted, as 2014 is an election year.

GCG: When talking to a client what are the key questions you are asking in order to properly put together the right strategy and portfolio?

Glover: In order to give the best advice to our clients, it is important to understand their business, but also how their teams interact, the way in which they prefer to communicate and their objectives for the future. Understanding a tax technical position is usually the smaller part of high quality advice. Obviously, any advice must be technically correct, but if the client can't understand the issue or the advice is not practical, there should be no surprise that it will not command a premium fee. Before we can talk with a client about their strategy, we need to build their confidence in our abilities and integrity. Any questions posed must keep all of the above in mind. We need to bring our experience to their particular fact pattern. No two client situations are exactly the same, but as experience builds the answer often becomes clear more quickly. ■

A practical approach to tax advice in Romania

Interview: Marius Ionescu, partner at Nestor Nestor Diculescu Kingsten Petersen Tax Advisory Services (NNDKP Tax) – Romania



Marius Ionescu has 15 years of experience in local and international tax consulting firms. His areas of expertise include investment tax structuring, tax planning, transaction advice, tax review and due diligence projects for large local and multinational companies. He is a Partner with NNDKP Tax Advisory Services and co-heads the division within the law firm.

GCG: Mr. Ionescu, thank you kindly for taking time out of your schedule to speak with us. Can you please tell our readers a bit about your background?

Ionescu: I am an economist working as a tax consultant for the last 15 years. I started in 1998 with Arthur Andersen, moved on to Ernst & Young in 2002 (after the Enron case fallout) and for the last five years I have been a partner with Nestor Nestor Diculescu Kingsten Petersen Tax Advisory Services (NNDKP Tax), which is the tax consultancy arm of NNDKP, one of the most important law firms in Romania.

GCG: You've managed to build the NNDKP Tax Advisory Services from the ground up and experienced a great deal of success. What kind of challenges did this entail and how did you manage to overcome them?

Ionescu: There are of course inherent challenges related to the growth

of a company. When I joined NNDKP in 2008 the tax practice had three professionals. Now we are 22. The turnover also increased proportionally. With such growth one has to deal with a lot of ingredients, such as building the right team of professionals, increasing the client's portfolio, taking great care of the brand awareness and firm's reputation, assuring a high level of quality of services rendered, and so on. My colleagues and I did all of these things on a daily basis. It was a great business experience and a very satisfactory and fruitful exercise. However, I guess the main change was at a conceptual level, specifically the move from an accounting firm to a law firm. Being a tax consultant in a law firm allows and requires a more practical approach and from this perspective a deeper involvement in the matters of advice. Lawyers not only advise their clients, but also draft the related agreements, being deeply involved in the negotiations of a transaction and also implementation of the respective agreements

as well as potential post-transaction litigations. From such a perspective, the approach of a tax consultant must be more practical and applied. To give an example, one of the things I started to do since I moved to NNDKP was to assist our clients as a judiciary expert in court, giving me the opportunity to deal with the aspects of tax litigation and enhance my experience as a tax consultant with this very practical perspective.

GCG: Your team is built around people with diverse backgrounds, including specialized economists, certified tax advisors, as well as tax lawyers. Do you find it a challenge to corroborate the many different points of view that they have to offer clients?

Ionescu: The educational background is obviously important, but at the end of the day we are all tax consultants in the same profession. However, having economists as well as lawyers on our team offers us the opportunity to have access to both professional perspectives when assisting our clients.

GCG: What differences do you see in the way that you handle tax matters for clients as opposed to the

way somebody with a legal background might handle them?

Ionescu: There are countries in Europe where only lawyers can act as tax consultants. Others, including Romania, allow advice by economists as well. In my view economists have their role in this profession as one cannot be a good tax advisor without a good understanding of figures and accounting. There are instances, and more than a few, when tax issues pop up from accounting rules. Lawyers on the other hand benefit from a holistic legal approach, which at times can prove useful in addressing a tax issue.

GCG: Being on a different side of the organization than the traditional legal practice, what type of interaction do you have with the other lawyers at the firm?

Ionescu: We work very closely with our colleagues in the law firm because the concept for us is a one-stop shop, meaning a place where the client can obtain premium legal and tax services in an integrated manner. The collaboration includes inter-alia, integrated advice on tax and legal issues, drafting transaction agreements and/or assisting clients on tax litigation matters.

GCG: In recent years, countries have made a distinct effort to reform tax codes in a manner that boosts national revenue with the goal of slashing deficits. In what way has new legislation affected your practice?

Ionescu: The work we are involved in has changed significantly from

the economic boom years. Back in 2008 a big part of what we did was related to investments and businesses changing hands, especially in real estate. Now we spend a good chunk of our time assisting clients during tax audits and/or litigations with the tax authorities. This is due to the fact that during the years of economic crisis the tax authorities have become increasingly aggressive given the need for income to the state budget. Therefore, our clients need premium assistance in this respect and we are proud to offer it to them.

GCG: How have changes in the tax code resonated with your clients?

Ionescu: We can talk of a constant increase of the effective tax rate in Romania, even if not a dramatic one (if we take apart the VAT increase by 5 percentage points in 2010). Various deductions and previously untaxed items have been drawn into the scope of taxes by new laws. In addition to this, as I already said, the tax authorities' approach during a tax audit moved to the rather aggressive side. Unfortunately, this means additional stress to taxpayers, who are already stretched by the economic crisis.

GCG: How does your organization distinguish itself with the services it provides to clients from other types of organizations, such as the Big Four consultancy firms?

Ionescu: Being a law firm, our advice can be much more practical and really oriented to the needs of clients – from the first phases of advice up to the litigation if need be. We see the effects of our advice during the implementation phase, which is a

Title: Partner with NNDKP Tax Advisory Service; co-heads the division within the law firm

Areas of expertise: Investment tax structuring, tax planning, transaction advice, tax review and due diligence projects for large local and multinational companies.

Career: 15 years of experience in local and international tax consulting firms. Started career in 1998 with Arthur Andersen, moved on to Ernst & Young in 2002 and for the last five years has been a partner with Nestor Nestor Diculescu Kingston Petersen Tax Advisory Services (NNDKP Tax), which is the tax consultancy arm of NNDKP, one of the most important law firms in Romania.

Background: An economist working as a tax consultant

Highlights: ince 2008 has helped grow the NNDKP tax practice from three to 22 professionals

On moving to a law firm: "Being a tax consultant in a law firm allows and requires a more practical approach and from this perspective a deeper involvement in the matters of advice. Lawyers not only advise their clients, but also draft the related agreements, being deeply involved in the negotiations of a transaction and also implementation of the respective agreements as well as potential post-transaction litigations. From such a perspective, the approach of a tax consultant must be more practical and applied."

helpful experience for a tax advisor. We are also able to offer high-quality integrated tax and legal advice within the one-stop-shop concept.

GCG: NNDKP Tax Advisory Services deals with a variety of taxation matters, including planning, structuring, litigation and compliance. Which area do you find most challenging and why?

Ionescu: Definitely litigation. It is extremely challenging and rewarding to see your opinions validated by a judge. Plus, you are making a client happy at the same time.

GCG: You deal with businesses in a varied range of sectors, such as energy and utilities, pharmaceutical and banking and financial. Which do you find the most interesting to work with and why?

Ionescu: All industries have their interesting parts and specific is-

ues. It is difficult to get bored as a tax consultant. For instance, I was heavily involved in real estate during the economic boom, now I deal a lot with automotive, banks or retail, just to name a few industries.

GCG: There has been a great international debate about how governments can successfully foster a productive and beneficial environment for businesses to thrive in, a part of which is an effective tax code. How do you think Romania has done in creating such an environment?

Ionescu: Romania keeps its attractiveness from a tax perspective, with a 16 percent income tax rate. Both government and business associations want to create a better business environment, however the results are rather scarce so far, due to the current adverse economic climate.

GCG: For a young person who wants to specialize in tax consulting services and perform duties along the lines of yours, what sort of a career path would you recommend? Would you recommend accounting or the law?

Ionescu: Any of it would be fine. It takes at least 10 years to become a tax consultant in the real meaning of the word. It takes a long time to learn. As I said, the trip is not boring though.

GCG: Finally, if you could go back to when you were just coming out of university and give yourself some advice, what would you tell yourself?

Ionescu: This is a difficult question. Looking back, I am pleased with how things developed. I think I made the right choices at essential moments. One always needs a bit of luck, but the main part of it is about hard work and dedication. ■



Downtown Bucharest

Tackling the toughest tax code

Guilherme Donega

Tax Manager at GE – Brazil

Guilherme Donega is an attorney, responsible for audits, litigation and tax compliance for GE in Brazil. This means that his daily job is to deal with the most complex tax legislation in the world that involves an archaic tax system with a mix of digital tax returns. The result is often microscopic validations of every single tax aspect of business. It should also be noted that Donega carries out his role in one of the most litigious countries in the world.

GCG: Your career track has been a fast one. Can you give our readers a brief overview of how you got to where you are today?

Donega: I have joined GE in 2008 after a couple of years as an intern in private practice. Being part of a law firm is truly a terrific experience and I recommend it to every lawyer. When I was part of that world, however, I felt overwhelmed by the diversity among our clients and distant from the things they did. So I decided to join the other side of the table and came to GE to become part of the legal team.

About five years later and having passed through different roles in several GE businesses areas, I can only look back and cherish that decision. Big companies are fertile ground for career development for those willing to commit the time and effort and GE is no different.

Being focused on results, clear communication and high standards will get professionals moving fast on their career. With this in mind, I moved from Legal to Tax, from intern to attorney and from attorney

to manager in less than five years.

GCG: GE is huge and extremely diverse corporation. Can you tell us a bit about your role in the company?

Donega: Beginning in 2013 I have managed an area responsible for part of GE's tax compliance in Brazil: tax audits attendance, litigation and compliance monitoring. This team is part of a shared center that delivers tax compliance services to GE business units in Brazil.

Basically, my job is to guarantee that GE business units are adopting tax efficient compliance, to the extent of GE's tax positioning and to support our compliance when going through external audits. If everything goes wrong and GE comes out of a given audit with a tax assessment, the team I manage is also responsible for appealing that tax assessment under administrative courts.

But the great thing about working for GE is that we actually make great things. If you are brave enough to get out of the office in Sao Paulo and go to a GE business unit facility you



get to see how GE equipment changes the world: healthcare machines, wind turbines, oil extraction equipment and so many other solutions that the world really needs.

GCG: A recent article in The Economist described tax disputes in Brazil as being as common as "string bikinis and Samba". What issues are you facing?

Donega: A recent study pointed that there is at least (U.S.) \$230 billion in federal tax disputes at stake in Brazilian judicial or administrative courts. As we follow a three-level taxation system (federal, state and municipal taxes), you can add to this number some significant state and municipal exposure.

But even if you disregard that fact, \$230 billion is 15 percent of Brazil's GDP. For comparison, in the United States, the IRS stated that there is \$40 billion in dispute, or 0.2 percent of the country's GDP. Not only is the amount in discussion high, but the number of existing tax lawsuits is also scary. In Brazil, there are 16 tax lawsuits for each 10,000 inhabitants; in Canada there are two for each 10,000.

Inside those disputes there is an enormous quantity of topics being discussed: from taxation of international profits of Brazilian companies to electronic bureaucracy formalities fulfillment, from goodwill amortization to transfer pricing calculations, most of Brazilian tax matters are subject to lawsuits. If it is in the tax legislation, chances are that someone has already litigated over it.

GCG: The World Bank rates Brazil's tax code as the world's most complicated. Do you agree? If so, why is that and how do you navigate it?

Donega: I surely do. There are 88 taxes in place in Brazil right now. If that does not sound complicated, keep in mind the federal government, plus all 27 states and 5,560 cities can issue their own rules about the taxes they manage. This results in about 46 new tax rules every single day. As there are so many new rules, some of them tend to conflict with either the Tax Code, the Federal Constitution or any other existing tax law. This leaves a lot of room to litigate.

Managing so much complexity is not easy. First, you need a lot of creativity to see the system as a whole, while keeping in mind that each tax is specific. Second, as you have stated, Brazil is the country in which companies spend the most time among the entire world to comply with tax obligations: 2,600 hours per year. Second is Bolivia, with 1,025 hours. So you also need a large team to manage tax compliance.

GCG: As a follow up to the above question, what does Brazil need

to do, in your opinion, to improve and streamline its tax system?

Donega: Brazil needs to understand the impact our tax system has on companies. Big companies can afford to have tax professionals that will try to achieve tax efficiency. Small and medium sized ones cannot. These last two are more than 90 percent of the number of Brazilian companies and represent around 20 percent of the country's GDP. Do you think they can also manage their taxes wisely in this heavily complex system?

Brazilian tax authorities must start to see taxpayers as partners, not enemies. Tax revenue has been going up for years now as the investments in the country are growing. Businesses are leaving the formal economy and the demand for consumption is growing. This fertile ground will reach its limit and the only way to go beyond it will be through changes on how tax authorities sees taxpayers: tax revenue will only grow further if businesses are growing; and business will only be growing if they can partner with tax authorities to achieve simpler tax compliance environment. Lastly, the country needs to have the courage to change what is not working. The three existing tax entities do not necessarily feel comfortable with the taxes they get today, but they at least know how much revenue they will have at the end of the month. Each one of them is afraid to lose this predictable revenue with a change in the tax system, but if no one shows the will to change how things work, Brazil will keep ranking first in the World Bank study forever.



GCG: Much has been made of how tax authorities in Brazil approach audits. Can you explain their approach to our readers?

Donega: We can split Brazilian tax audits into two kinds: crosschecks and positioning audits. Having the most complex tax system worldwide makes returns hard to file and prone to errors. Once your returns go to the tax processing system, the authorities crosscheck the returns with other returns that should have matching information, be it submitted by third parties or by yourself.

For instance, you have at least a couple of taxes that are levied over companies' income with separate returns for each of them. They should have matching information; if they do not (and sometimes there are

reasons for the mismatching), the IRS will send an auditor to check the tax calculations in detail. As our legislation demands strict tax controls, it is common to have auditors going through thousands of invoices, returns, balance sheets and contracts. Because of that, it is not uncommon to have audits lasting for years. And as auditors are usually looking at two to three year old returns, you must imagine how hard it can be to go through the company's records and find the proper documents – sometimes there are more than 50 people going through rooms full of boxes of documents to find what auditors request in a five to 20 day deadline.

Other than those crosschecks, there are also cases where tax authorities decide to dive deep into a specific tax positioning adopted by a given company. Usually, tax authorities interpret the existing legislation in a way that results in a greater tax revenue for them, stating that any positioning different to theirs is abusive (even when judicial courts have already stated they are not). Once they think that a taxpayer is taking an abusive tax approach, they open audits to check it and ultimately challenge it.

GCG: Has electronic filing helped the country in any way or simply made things more complicated?

Donega: Electronic filing has been in place for some time now, however the way it was implemented did not help make compliance any easier, it only helped tax authorities to find more and more issues to audit.

In recent years, electronic returns have gone through changes. Federal

tax authorities partnered with states and decided to revamp the electronic returns with the goal to give complete access of the companies' controls to the IRS.

The idea itself is not all bad as it could help to minimize hours spent in tax compliance by automatizing a lot of manual work. However, I see a couple of problems with how the idea is going so far: first, these new electronic returns coexist with the old returns, basically doubling the necessary time to file them. Second is that once your compliance is fully open to the tax authorities they can get to know the tax positions of companies, for each individual operation they do. Once the authorities disagree with a given tax treatment, they could issue a tax assessment electronically, without giving a chance for a company to justify its positioning on audits, meaning they have to defend themselves in court.

GCG: Is Brazil's byzantine tax system resulting in less foreign investment in the country?

Donega: I cannot say on behalf of GE, but in general, it is my personal impression that Brazilian tax environment indeed does drive investment away from the country. Brazil has been lucky for a few years due to high demand for consumption, especially among the lower classes. With this level of demand the tax environment was not a roadblock for investment. Everyone was investing in Brazil, so why should a company go elsewhere? However, once this demand stabilizes and companies need to choose between

similar markets, I tend to believe that they will choose one with the most predictable tax environment.

GCG: What advice would you give to foreign companies looking to do business in Brazil?

Donega: Hire a Brazilian tax expert. If he tries to explain something you do not understand, be patient.

What are the biggest challenges and rewards of your job?

Donega: As for the challenge part, I think it is the balance between prioritization and focusing on details. When you are constantly dealing with more than 30 tax audits, 20 tax appeals and several internal compliance validations, you must have the skill set to focus on what is important. Notwithstanding, you must validate every interaction you make on audits and appeals in detail because they will be analyzed by auditors. Navigating Brazilian tax complexity can be a challenge, but feels very rewarding once you get to solid ground and see the path you sailed.

Beyond that, I am also really proud to work for GE and to be pushed on a daily basis to deliver results with the highest standards. And to know that at the end of the day, I have guide GE in this complex scenario and allow the company to conceive new solutions to the world's toughest challenges. When you compare problems like healthcare and ecological power generation to Brazil's tax environment, you could say that what I deal with daily does not even come close to the world's real problems. ■

Big Deals

A roundup of major recent transactions and the firms that put them together

DLA Piper advising a top Brazilian pulp producer

DLA Piper Hungary is advising a top Brazilian pulp producer on relocating its sales operations from Hungary to another jurisdiction. The team provided tax and legal assistance in the process of the restructuring. The tax work was highly complex and innovative. For instance, compared to ordinary TP methods an alternative method was introduced to support the arm's length nature of the transaction.

Kinstellar has handled several recent deals

Columbian Chemicals – Tax deductibility opinion

Kinstellar advised Columbian Chemicals (a U.S. carbon black manufacturer with substantial operations in Hungary and part of the Aditya Birla group, a diversified Indian industrial conglomerate) in connection with a tax opinion prepared for U.S. tax and accounting purposes. The opinion addressed the Hungarian tax deductibility of interest expenses incurred in connection with a complex back-to-back group financing and repatriation transaction.

BNP Paribas – Cross-border factoring opinion

Kinstellar advised BNP Paribas (a leading global bank) in connection with the Hungarian tax implications of structuring a cross-border factoring arrangement aimed at refinancing receivables of Hungarian businesses.

MOL EMTN Program

Kinstellar advised Citigroup Global Markets Limited and HSBC as dealers in connection with a \$1 billion guaranteed medium term note program set up by MOL (the Hungarian energy major) to be listed on the Luxembourg Stock Exchange as well as in connection with the first \$500 million offering of seven-year maturity U.S. notes under the program including tax implications.

Corporate bond by Nitrogénművek

Kinstellar advised BNP Paribas and Raiffeisen International as joint lead managers in connection with the \$200 million offering of seven-year maturity U.S. notes paying an annual fixed 7.875 percent interest by Nitrogénművek Chemicals (a major Hungarian artificial and fertilizers business) to be listed on the Luxembourg EURO MTF market.

Gide Budapest handling several notable matters

Advising Servier Group on its voluntary public purchase offer

Gide Budapest advised Servier Group on its voluntary public purchase offer of EURO 358 million for all outstanding shares of Egis Pharmaceuticals Plc., a company listed on the Budapest Stock Exchange. The deal is the largest capital markets/M&A deal in Hungary with many novel complex aspects, which have not been encountered in previous similar transactions.

Advising a major bank on the securities of a syndicated loan

Gide Budapest advised on the security documents of the syndicated loan agreement in which the bank participated. A participation in a syndicate loan was transferred to the client on the secondary market who was also appointed as agent of the bank syndicate.

Advising on the development of an office building in Budapest

Gide Budapest advised a major bank in connection with the real estate development of an "A" class office building in Budapest, which included the drafting of the entire financing documentation and other related project documents.

Allen & Overy has wrapped up several deals across Europe

Hungary: Represented MKB Bank in a successful litigation. Allen & Overy represented MKB Bank in court proceedings regarding its claims exceeding EUR 25 million under a direct agreement against the Hungarian Metropolitan Municipality. The court ruled that the agreement was valid and enforceable and not contrary to EU state aid rules. This is the first time a direct agreement has been tested before the Hungarian courts.

Romania: RTPR Allen & Overy advised JP Morgan on the largest Romanian corporate bonds issuance to date. The deal was in relation to the issuance by Cable Communications Systems N.V. (CCS) of EUR 450 million Senior Secured Notes guaranteed by RCS & RDS S.A., a leading provider of pay TV services in Romania and Hungary.

Poland: Allen & Overy advised Neoświat PPP, part of the French group Bouygues, on a PPP project in Poland that included the development of Jagiellonian University

student dormitories. This is the first PPP project in Poland involving a public university and also the first such venture in the public building sector.

Czech Republic: Allen & Overy led Colfax Corporation's acquisition of ČKD Kompresory. Colfax is a leading global manufacturer of gas- and fluid-handling and fabrication technology products and listed on the NYSE. The \$57 million acquisition of ČKD Kompresory, based in Prague, Czech Republic, was from ČKD Group.

Nestor Nestor Diculesco Kingston Petersen (NNDKP) Tax Advisory Services has handled several recent tax-related matters, including

Tax advice on the restructuring of an agribusiness investment

NNDKP advised an important foreign investment fund on the Romanian tax implications relevant for the restructuring of its agribusiness investment. The deal comprised several jurisdictions and four local companies and also provided full assistance in relation to the observance of the local tax compliance requirements imposed by such restructuring.

Advice on tax procedures for a significant player in retail

NNDKP designed the tax procedures in relation to the inventory management and stocktaking for a major player in retail. The delivery

consisted of a procedure mapping dealing with relevant profits tax and VAT aspects.

Tax advice in a cross-border merger of a major bank

NNDKP assisted an important international bank in a cross-border merger between its Romanian subsidiary and the UK headquarters. The firm advised on all tax implications related to such a process, including implementation advice.

Advice on tax restructuring in a major privatization in the automotive industry

NNDKP assisted a major automotive company in Romania through-out the finalization of the privatization process (the last stage of the process started in 2008). The assistance included the final tax restructuring of the privatized company as well as complex negotiations with the state authorities for finalizing the process.

Țuca Zbarcea & Asociații advies on largest Romanis office deal

Țuca Zbârcea & Asociații's real estate team advised U.S.-based Electronic Arts, Inc. in concluding a long-term lease agreement with real estate developer AFI Europe on the leasing of 11,500 sqm of office space. According to media reports, the total rental value exceeds 14 million Euros and the deal is the largest of its kind in the country.

Țuca Zbârcea & Asociații also advised Getin Holding on its Romanian market entry

The firm acted on behalf of the Polish financial group Getin Holding as it sealed its first deal in the Romanian market, through the acquisition of the full 100 percent stake in the Romanian International Bank (RIB), a local lender dealing with individual clients and small- and medium-sized enterprises.

Navigating Austria's complex tax environment

By Cassandra Yashpal



Behind every map, there is a much more complex map, which often holds the key to your queries, but is also hidden from your view. I guess the same could be said for every business striving to find the right elements to make it a success.

Coming from a city like London and having worked for one of the “Big Four” and now living in Austria, I feel a little like the needle in the compass, navigating my way. Why, you ask? Well, it all comes down to the fact that I, like a lot of other people, am looking from the outside in when it comes to Austria or, in fact, any other CEE market. The Tax environment within Austria is more complex and offers an increasingly fascinating insight that is more than most of us could actually imagine.

About 13 years ago, one had the ability to talk to an auditor and a reasonable and beneficial outcome for both the taxpayer and the revenue could be established when determining both the structure and the tax planning opportunities for most businesses. Fast-forward six years and things have changed – and not necessarily for the better. When it comes to businesses and auditing, there seems to be less agreeability and amicability in terms of reasonable solutions for both the taxpayer and the authorities.

Imke Gerdes, one of the few Austrian lawyers qualified as both a lawyer and a tax advisor (“Steuerberater”)

for Baker & McKenzie said that, “to a large extent, this started with the general budget pressure and the reorganization of the Austrian Tax Authority. A few years ago, the Austrian authorities installed focus groups, such as a group specialized in transfer pricing. Instead of dealing with the general auditor, one had to deal with tax officials that specialized in this area. A positive effect is that discussions are lead on a more sophisticated level. However, paired with general budget pressure, one sometimes has the feeling that the authorities use this knowledge to generate more taxes and not to find a reasonable solution for the tax payer as well as for the revenue.”

In terms of challenges faced within the Austrian tax environment, Niklas Schmidt who is qualified as both a lawyer and tax advisor and is a partner with Wolf Theiss, one of the first Austrian law firms to advise on national and international tax law said, “everything is becoming more of a level playing field. The advantages that advisers had are eroding. In the past, many tax auditors did not speak English well and had a low level of tax education. Now, everybody in the administration speaks English well, our opponents have become a lot more professional, their possibilities to request information from other tax authorities, in particular in tax havens, have vastly improved, the Organization for Economic Cooperation and De-

velopment (OECD) is helping tax authorities with many initiatives.”

Schmidt added that as of Jan. 1, 2014, Austria will introduce courts for tax matters. “This will offer a more professional conduct going forward as the existing administrative body for appeals will be replaced by a true tax court (Bundesfinanzgericht). It is expected that this will help improve the appeals procedure for taxpayers.”

When looking at various challenges faced when building a tax practice in Austria, there have been some interesting and varied views ranging from one end of the spectrum to another. On one hand, the recruitment market for Austria and building a tax practice has been a main focal point. The educational system has changed in the last two years as well as admissions systems. Ultimately, as Dr. Michael Sedlaczek, a tax partner for Freshfields Bruckhaus Deringer, mentioned, “at the end of the day, ‘quality over quantity’ is valuable”. Baker’s Gerdes had this to say, however: “Baker & McKenzie are looking to build up an Austrian office. If you are solely an advisor and not admitted to the bar, you may not become a partner in a law firm, as Austrian bar rules do not allow interdisciplinary partnerships. Therefore, we are looking for dual-qualified people and that limits the pool

of possible recruits. However, if you are dual qualified as a candidate it is easier to find employment as you will have a wider skill set.”

One of the biggest elements Austria, as a member of the OECD, has faced and continues to face is the fight against tax evasion and tax fraud. When speaking with Robert Schneider, general partner and founding partner of Schneider’s Rechtsanwalts-KG, he said that, “within the last three years, it has become very difficult in terms of tax law. We used to be able to practice under international tax law, but this has now been stopped as a consequence of the international discussion on base erosion and profit shifting. At a recent conference, the main area of new focus was directed at defense strategies and criminal tax law”.

One of the most significant recent political themes in the area of international taxation is the attempt of the international community, e.g. OECD and EU, to tackle international tax evasion and tax fraud.

Freshfields’ Sedlaczek gave this view: “Austria has strongly been participating in these international movements, particularly in the context of the OECD, e.g. on the development of transfer pricing guidelines and the development of the commentary of the OECD model convention on the avoidance of double taxation.

International developments in that area, e.g. BEPS (base erosion and profit shifting) are supported by Austria. Somewhat unjustified on the other hand, Austria has been put in the corner of a “tax haven” on the basis of the protection of the confidentiality of individual data, such as under the banking secrecy, which some people believe only lends itself to tax fraud. In that context, however, Austria has concluded cooperation treaties with Switzerland and Liechtenstein (coming into force as of Jan. 1, 2014), which are intended to tackle tax fraud by Austrian resident individuals, both for the past and the future.”

The agreement between both Liechtenstein and Austria corresponds to

the existing agreement with Switzerland, but has a broader scope. The ultimate aim of this agreement comprises taxation from previous untaxed entities, but ensuring taxation of future investment income and capital gains. With the continuing changes to tax in Austria, legislation has now made it more complex and difficult when faced with opportunities of tax fraud and evasion. Necessary risk management and strategies targeted towards tax are very much a daily necessity.

It doesn’t have to be complicated to address tax fraud, evasion or tax as whole. UK tax law consists of seven books and tens of thousands of pages dedicated to ensuring the UK resident pays their fair share of tax and recent additional legislation introduced by the UK government seeks to attack aggressive tax planning opportunities. While Austria is in some ways similar to the draconian UK tax system I hope fervently that this is not a direction they are heading towards.

When looking from the outside in, we need to take into account that things are often not what they seem. With the right attitude, hard work and dedication, however, one can always strive to meet any challenges he or she may face. Tax should be no different.

Cassandra Yashpal is an Associate Consultant with a Tax focus who joined Legalis Global in October 2013. Cassandra’s main focus is on tax lawyers and tax-qualified candidates through-out the Emerging Markets.



PIS and COFINS and the creditable expenses



By Vanessa Inhasz Cardoso



PIS and COFINS are social contributions levied on gross revenues. Currently, in Brazil, there are two different regimes to calculate and pay these taxes: cumulative and non-cumulative regimes. Under the cumulative regime, PIS and COFINS tax rates are lower: 0,65 percent and 3 percent, respectively and no credits are allowed. In the non-cumulative regime the tax rates are higher: 1,65 percent and 7,60 percent respectively, but certain credits can be deducted from the taxable basis of the contributions.

This kind of system is also applicable for the State VAT (ICMS) and Excise Tax (IPI). Although the PIS and COFINS non-cumulative system is different from the VAT and IPI regimes, one can say that the intention of both systems would be the same – i.e. to avoid the levy of tax over tax and reduce the tax burden of the manufacturing sector.

PIS and COFINS legislation sets forth that the companies are entitled to credits related to these contributions in the following operations: (1) acquisition of goods for resale, except goods and services expressly mentioned in the legislation; (2) acquisition of goods and services for use as input in the rendering of service and in the manufacture of products, including fuel and lubricants; (3) electric and thermo power, also in steam form, used in the company's operations; (4) payment

of leases of buildings, machines and equipment used in the company's operations; (5) lease expenses derived from leasing transactions, except for companies under the SIMPLES regime; (6) acquisition or manufacture of machines and equipment acquired or manufactured to be leased to third parties or used in the manufacture of products intended for sale and of other goods incorporated to the fixed assets; (7) buildings and betterments in third party real estate property to be used in the company's operations; and (8) return of goods.

While most of the aforementioned situations are pretty much clearly stated in the legislation, the acquisition of goods or services used as inputs in the manufacturing of goods for sale or for service rendering it is not clearly defined. This results in a lot of discussion between the taxpayers and the Federal Revenue Department.

There is no definition in the law on the concept of input. The concept was defined by Normative Rulings #247/02 and #404/04 issued by the Federal Revenue Department as the raw materials, intermediate products, packaging materials, and any other goods that suffer changes such as wear and tear, damages, or loss of physical and chemical properties due to the action directly exercised on the product being manufactured.

The concepts set forth in those Normative Rulings were inspired in the legislation and administrative rulings that deal with inputs for the purposes of IPI credits, which is a tax with totally different features from PIS and COFINS.

We believe that it is not adequate to tie PIS and COFINS credits to the effective application and use of inputs in the final product or rendering of services, due to the loss of physical properties, wear and tear, etc. The credits should be tied to the expenses required and inherent to the business, which generates revenues for the company.

The issue is very controversial and the case law is not settled yet. There are three basic positions under dispute. In the first, very restrictive one, the concept of input should be the same adopted by the IPI legislation (i.e. effective application and use of inputs in the final product or rendering of services). In the second, very broad one, the concept of input should follow the Income Tax legislation (i.e. all expenses incurred by the taxpayer that are necessary to carry out its activities should be creditable for PIS and COFINS purposes). The last one represents an

What are PIS and COFINS?

A Brazilian construct, PIS and COFINS are two complex social contribution taxes levied on gross revenues that have been the cause of much debate in Brazil. The taxes resulted in a polemic debate in Brazil after taxation reform efforts proposed the unification of both as single tax.

intermediate approach, in which the criteria to define whether an expense should be creditable is the relevance and necessity to the manufacturing process/rendering of services or the essentiality of the expense to generate the revenues that will be taxed by PIS and COFINS.

Although the understanding of the Federal Revenue Department has evolved over the past years it still adopts a very restrictive position

(especially in decisions on Requests for Rulings) and it has been assessing the companies that do not share the same position.

As to the case law, there are decisions addressing all the aforementioned positions, but the most recent ones rendered by the Administrative Court of Tax Appeals (second Administrative Court level in Brazil) are following the intermediate approach, i.e. based on a case by case

analysis considering mainly the relevance and necessity of the expense to the manufacturing process/rendering of services and generation of revenues to the company.

We understand that the non-cumulative regime of PIS and COFINS is unique and should be treated accordingly and the intermediate position is the one that most reflects the rationale behind the PIS and COFINS non-cumulative regime. We believe that this approach will most likely prevail in administrative and judicial Courts.

Vanessa Inhasz Cardoso is the head of the International Tax Consulting Department of Lima Junior, Domene Advogados Associados.

Dividend taxation in cross-border transactions with Czech shares



By Aleš Zidek

Under Czech corporate law, a shareholder of a company is entitled to a share in the company's profit, which the company's general meeting approved to be distributed (dividend). The dividends distributed by the Czech-resident companies to the non-resident shareholders are generally taxable in the Czech Republic. The dividend tax is collected by withholding at the source.

A standard dividend tax rate is 15 percent. If a shareholder is resident in a jurisdiction outside the EU, the

EEA, and the states, which have a double taxation treaty or a tax information exchange treaty in force with the Czech Republic, the tax rate is 35 percent.

The Czech Republic has a wide double tax treaty network. The tax treaties prevail over the domestic law, and many reduce the dividend tax rate to 10 percent or 5 percent, some even to 0 percent for qualifying recipients, typically in cases of under a minimum shareholding percentage.



Beneficial ownership and anti-abuse

Under Czech tax law and the tax treaties, the dividend income is attributed to the beneficial owner of the shares on the dividend record date, which is generally the date of the general meeting, which approved the dividend for distribution. A beneficial owner is defined as a recipient who receives the dividends for its own benefit and not

as an intermediary, representative, or agent of another party. Official interpretations distinguish between an immediate recipient and a beneficial owner by referring to the taxation of the corresponding income at the level of the beneficial owner. The shareholders need to confirm their beneficial ownership status to the company paying the dividend income in the form of an affidavit.

Czech tax case-law also applies the anti-abuse principle, applicable generally to transactions resulting in unjustified tax saving to parties involved while typically being fully or largely tax-driven. Consider a transaction where one party (having access to a low treaty rate) purchases securities from another party (not being eligible to such rate, such as, for example, a Czech resident) prior to the dividend record date, making it contractually insulated from a risk related to holding the share and then sells the shares back after the dividend record date. In such a case, the former party might not be granted any tax relief, either as a result of not being a true beneficial owner or as a result of being involved in an abusive transaction.

Financial transactions with Czech shares

Stock loans

In a typical stock loan, the stock borrower assumes full legal title to the shares borrowed and the stock lender receives cash collateral. At the dividend date, the stock borrower receives the dividend and pays the stock lender an equivalent thereof, a 'manufactured dividend'. At expiry, the stock borrower returns the

shares to the stock lender, and the stock lender returns the cash collateral, while both may involve an element of interest.

The stock borrower should qualify as the beneficial owner of the dividends received on the shares borrowed, while the manufactured dividend payable to the stock lender should not impede his beneficial ownership. This assumes a bona fide commercial transaction where the stock borrower would typically not be limited to dispose with the shares and would be entitled to all the rights attached to the shares and all the benefits and risks of holding the shares.

While no official interpretation is available in respect of the manufactured dividend itself, it will likely be regarded as Czech-sourced income, taxable – under Czech laws – essentially with the same 15 percent/35 percent withholding tax as a dividend. A tax treaty may then provide a protection for the non-resident recipient, either in the form of a 0 percent treaty rate or in not qualifying the manufactured dividends as business profit or other profit, both of which are typically also protected from Czech taxation under the tax treaties.

Derivatives

While there can be numerous derivative transactions using Czech shares as the underlying asset, a good example would be a total return swap (TRS). Under a typical TRS, the one party ('long party') pays a fixed return agreed under the swap; the other party ('short party') pays a return equivalent to full re-

turn on the underlying shares, including dividends. While the TRS does not require either party to hold the underlying shares, there may be situations, such as hedging, in which the short party to the TRS at the same time holds the underlying shares.

The short party to the TRS should qualify as the beneficial owner of the dividends received on the shares it holds, while the payment to the long party to the TRS should not impede its beneficial ownership.

A more specific official interpretation is available with respect to payments under TRS, and generally in respect to any similar payment under derivative contracts. Such income should be taxable essentially as income similar to interest, subject to 15 to 35 percent withholding tax under the Czech tax law. Under a tax treaty, it would typically be exempt as business profit or other profit.

We note that the tax treatment of income related to financial transactions depends greatly on the facts and circumstances of each particular case. Also the judgment of the Czech authorities may develop over time and may be difficult to anticipate due to the factors typical for the Czech tax environment, including the lack of specific guidance and frequent changes in the tax laws.

Aleš Zidek, head of White & Case Prague tax team, specializes in mergers & acquisitions and reorganizations, with a special focus on the energy industry, private equity, international tax, as well as general Czech corporate and personal tax consultancy.

Exchange of information: where it stands and where it goes



By Csővári István



Almost every week a new piece of information is published on the development in the ways tax authorities can exchange information between each other. It is not a surprise that taxpayers are unable to follow these developments. The most common questions raised by taxpayers on this topic are: what information can be provided by non-Hungarian tax authorities to Hungary?; can exchange of information apply even to events that happened before a treaty was signed?; what is the difference between exchange upon request and automatic exchange information?; do information exchange provisions also apply to companies held beneficially by individuals?

In this series we wish to give a thorough analysis of the topic. This first part deals with those options that are based on a treaty or an agreement of the relevant countries. In the second part, which will be published at www.gcgrapevine.com we will discuss the exchange of information legislation applied at the level of the European Union.

Automatic information exchange; exchange upon request

Before we move into the depth of the topic we need to understand the key difference between automatic and “upon request” information exchange. Normally, tax authorities exchange information with other countries’ authorities upon the request of

the other country. This means that tax information is only passed upon the request for specific information regarding a specifically identified taxpayer. The “upon request” information exchange does not authorize tax authorities for non-specific data fishing. Therefore only those persons may be worried of this type of information exchange against whom a tax investigation has already been started by their local tax authorities.

As the other main alternative, automatic information exchange becomes more and more frequent between tax authorities. In the framework of automatic information exchange the tax authority of one of the countries collects financial information that may be relevant for the other country’s tax authority and passes over such information without specific request. Obviously, this method of exchange of information can be the most frightening for taxpayers who want to hide their income and assets from their own tax authorities. While automatic exchange of information is not yet widespread, there is a strong pressure towards this way of cooperation from the Office for Economic Coordination (OECD) and the EU.

Treaty-based information exchange

Double tax treaties

Hungary entered into about 75 double tax treaties and all of these treaties contain a provision on exchange of information.

Normally, the treaties allow an “upon request” exchange of information. Although the treaties provide the legal basis for automatic exchange of information as well, in practice only a few countries adopt this method. On the basis of a survey the OECD conducted in 2012, currently 14 countries provide automatic tax information to the Hungarian tax authorities. The identity of these countries is, however, not available publicly.

It should be kept in mind that the scope of information exchanged between the tax authorities is not restricted to certain transactions or to bank account details. Any information that may be relevant for tax perspective can be exchanged with the country’s tax authority also being able to request the identity of beneficial owners of companies’ incorporated in the other country.

The information exchange provisions can have retroactive effect. This means that even if, at the present, no double treaty exist between Hungary and the other country involved, Hungarian taxpayers cannot feel fully safe with hiding tax information in the other country: if, at a later time, Hungary enters into a treaty with the respective country then even today’s tax information can be collected by the Hungarian tax authority. This

About Exchanges:

Tax Information Exchange Agreements (TIEAs) were developed by the OECD Global Forum Working Group on Effective Exchange of Information to address harmful tax practices. The Agreement, which was released in April 2002, is not a binding instrument, but contains two models for bilateral agreements between countries.

A TIEA can do the following:

Provides for exchange of information that is “foreseeably relevant” to the administration and enforcement of domestic tax laws on the Contracting Parties. Information provided under TIEA is protected by confidentiality obligations.

Information requested can relate to a person who is not a resident of a contracting party.

Information is defined in an expansive manner to cover banking details, ownership details of companies/persons/funds/trusts etc.

is why the currently adopted treaty between Hungary and the United Arab Emirates created deep concerns for many Hungarian individuals who failed to declare their Emirates-sourced income in the past.

Tax Information Exchange Agreements

As a new phenomenon in recent years, more and more “tax haven” countries started to enter into so-called “tax information exchange agreements” (TIEAs) with high tax countries. Tax haven countries are entering into such agreements in order not to be listed on the OECD blacklist, which would trigger various disadvantages to these countries.

These agreements contain similar provisions on exchange of information as double tax treaties do. A key difference is, however, that, as opposed to the double tax treaties, no retroactive information can be collected on the basis of these agreements.

To date, Hungary has entered into such an agreement with Guernsey only, but the Hungarian Government is authorised to negotiate TIEAs with almost all tax haven centres, like Lichtenstein, Andorra, Jersey, British Virgin Islands or Bermuda.

The OECD multilateral treaty

As a recent development, on Nov. 12, 2013, Hungary joined the OECD Multilateral Agreement On Mutual Administrative Assistance In Tax Matters. The treaty has 61 Member States, with Belize being the only member coming out of traditional tax haven countries. It is also noteworthy that about a month ago Switzerland also joined this treaty.

The objective of the treaty is to provide a platform for cooperation between tax authorities. Apart from allowing an “upon request” exchange information the agreement itself does not oblige tax authorities for a deeper cooperation but, based on the treaty, various exchange of information mechanisms can develop between the member countries.

The Swiss Rubik Agreements

The concept of Rubik Agreements became well known recently when Hungary indicated its willingness to enter into such agreements with

Switzerland. Up to now only the United Kingdom and Austria entered into such agreement with Switzerland, but Switzerland has expressed its willingness to enter into a Rubik agreement with any other countries.

The Rubik Agreements offer three alternatives for nationals of other countries having bank accounts in Switzerland. First, such persons can move their savings to another country without any sanction. Switzerland will, however, provide information to the home country of these persons on the 10 most preferred locations where such persons moved their funds to, so that the home tax authorities can follow where to locate these funds. As a second alternative, the bank account holder can opt for the deduction of a one-off, 30-35 percent tax from the savings placed in the Swiss bank account. The majority of this tax would be transferred from Switzerland to the home country of the bank account holders. Finally, if the account holder does not choose any of the options above, then the Swiss tax authorities will automatically exchange information regarding the identity and the bank account details of the holder with the home tax authority of such person.

In the second part of this series we will analyze the EU-based agreements as well as conclude as to whether there are any safe places still open for individuals or companies to hide financial information from the eyes of their home tax authorities.

Csővári István is an attorney and a registered tax expert, who has been working with the Jalsovszky Ügyvédi Iroda law firm in Hungary as a senior tax lawyer since 2006.

Is Romania a future business hub of Eastern Europe?

By Gabriel Biris and Ioana Cârțite



For the last couple of years the Romanian government has initiated various tax measures meant to attract foreign investors and to develop their long-term operations in Romania. In fact, as we will try to highlight below, all these initiatives have put our country on the map of the European countries with the most favorable holding legislation, on the same level with well-known countries like the Netherlands, Cyprus and Luxemburg.

In order to answer the above question, we need to first present the corporate income tax rate of 16 percent, one of the most competitive taxes in all the EU member states. Only Bulgaria and Cyprus (with 10 percent) and Latvia and Lithuania (with 15 percent) have a lower rate. This 16 percent rate has been applicable since 2005 and looks like the Romanian government will keep it unchanged for the following period. This actually contributed a great deal to the stability of the Romanian corporate taxation environment and, consequently, is one of the factors that will certainly attract long-term investments in our country.

At the same time, the latest tax legislation amendments brought by our government with regards to the taxation of dividends and capital gains also sustain this softer approach, in which a long-term vision of foreign investments is encouraged, rather than a speculative approach that would have led to short-termism. The main reason behind all these is Romania's goal for the following years, namely its tax stability.

The recent amendments on the taxation of dividends highlight that dividends distributed by a Romanian company to a non-resident company established in a state that concluded a Double Taxation Treaty ("DTT") with our country, are tax-exempt if this non-resident company (either EU or non-EU member) holds minimum 10 percent of the Romanian company's share capital for a period of more than one year, as opposed to the two-year period, which was previously applicable.

These current provisions are actually more favorable than those of the parent-subsidary directive for the dividend-beneficiaries resident in EU member states, while for those from non-EU countries with which Romania has a DTT concluded, this exemption is very often more advantageous than the dividend tax rate stated in the respective DTT.

Similarly, the capital gains obtained following the sale of shares held in a company resident in Romania or in a country with which our country has a DTT concluded are tax-exempt if the beneficiary of these gains holds a minimum 10 percent of that company's share capital for a period of more than one year.

Regarding the countries for which these favorable measures are applicable, we have to mention the fact that Romania is one of the EU member states having the largest number of DTT concluded: 85. That includes all



EU countries, almost all the European countries, the United States and Canada, Australia, the largest four Arabian countries, 20 Asian countries, 12 African countries and two Latin-American countries.

Comparably, the Netherlands, Cyprus and Luxemburg, countries renowned for favorable holding legislation, have 95, 53 and 77 DTTs concluded respectively. We could say, therefore, that Romania has started to have its tax legislation comparable to that of the other EU member states.

Also, it is worth mentioning that the latest amendments have been done by a left-wing government, but these were also included in the former-right-wing government's program, which shows a unanimous approach of the Romanian politicians with regards to the holding taxation intended to be applied by our country. Therefore, in the eventuality of a government change, these measures will remain unchanged, thus contributing to the overall stability of long-term holding taxation in Romania.

To conclude, you might want to keep all eyes on Romania, as it shows high potential to become an important regional hub for the foreign investments, considering the latest amendments and its importance in Eastern Europe.

Gabriel Biris is a partner and Ioana Cârțite is a senior consultant at Biris Goran SCPA in Romania.

Tax inspection in Romania – a brief survival guide



By Gabriel Sincu



Clients, potential clients and friends in need often pose the question: “how can I survive a tax inspection?” They are entrepreneurs, executives and middle managers at private and state-owned companies. However, we never receive this question from the people working for the rival team, the Romanian tax authorities.

The conclusion here is very straightforward. During an inspection the power balance is totally tipped in favor of the tax inspectors, who benefit the existing legal instruments to be the winners in the majority of these games. So it is natural that taxpayers are looking for ways to improve their odds.

We present below a couple of ideas, which may help in case you are faced with such a situation, without pretending that we covered, even partly, the complex area of expertise needed in case of a tax inspection.

From our experience, there are two sets of competencies required from the person handling a tax inspection. The first one is in the area of emotional intelligence, meaning communication and negotiation skills that we are also using in our day-to-day business. The other refers to the actual technical skills, meaning a strong amount of expertise in the areas of tax legislation and tax compliance regulation. We cannot say that one set or another is

the most important in winning this game, but finding the perfect combination of the two may result in a positive outcome.

As the technical elements can be easily found in the expert literature, we focused below on the category of emotional intelligence and recommend the following.

- You have to establish a balanced working report with the tax inspectors, adopting a steadfast and respectful attitude, such as to draw from the very beginning the borders, which neither you, nor the tax inspectors have to cross. By adopting a humble attitude you will allow the tax people to push harder and cross the line, meaning that you have a disadvantage from the very beginning. On the other hand, an aggressive approach from your side has to also be avoided, as this will generate a negative reaction from the inspectors who will make use, more than necessary, of the legal instruments mentioned above.

- Demonstrate to the tax inspection team that you have sound knowledge of the relevant legislation. We all know that the more information we have, the more powerful we are.

Before things get started ask the inspection team about the “Tax Audit Notification (TAN)”, the standard document that has to be presented

15 or 30 days in advance as the case may be. Read it thoroughly and if there are elements, which are not in line with the legal requirements, ask the tax inspectors to redraft it and come back.

Take the benefit of this 15- to 30-day period and read the chapter Tax Procedural Code dealing with the tax inspection. You will find this information very useful for the process to come. When the first day of the actual tax inspection arrives, ask the tax inspectors to fill in and sign your General Inspection Register, as required by the law. Do this before any review of the documents. All these actions will make the tax inspectors aware that they are dealing with a taxpayer who knows the law and will force them to adopt a less aggressive attitude.

- Be diplomatic when asking for professional support. The law allows you to receive support from a lawyer or tax consultant during the inspection. In some cases it is recommended to keep your advisor hidden from the inspectors. Ask for support, but do not bring him or her into the conversation. The tax inspectors may think that you want to hide some problems and this is why you

brought the advisor in. However, there are cases when the aggressive attitude of the inspectors requires the presence of the lawyer or tax consultant in order to bring back the balance. Use your emotional intelligence in deciding how to proceed.

- Choose carefully your team members that will be the interface with the tax inspectors.

The golden rule here is, less is more. The fewer people dealing directly with the tax inspection lowers the risk of leaking contradictory or unnecessary information. In such cases, additional investigations can be started, resulting in more work and more stress with the inspection.

Moreover, bring in the front line people with experience who are emotionally strong. They will not have to worry or be uncomfortable with the tax inspectors, as this will raise further questions.

Last, but not least, we want to point out that a tax inspection is not finished the moment the tax inspection report is signed by both parties. You have the right to present your written point of view, to appeal their decision or, if need be, go to court.

Good luck!

Gabriel Sincu is the executive director of Tax Advisory Services at Ernst & Young in Romania.

Keys to dealing with a tax inspection

Adopt a steadfast and respectful attitude

*Avoid an aggressive approach
Demonstrate sound knowledge of relevant legislation*

Read the Tax Procedural Code section on inspections

Make sure the tax inspectors to fill in and sign your General Inspection Register prior to document review

Be diplomatic when asking for professional support so as not to make it seem like you are hiding anything

Don't bring in an army of people – less is more

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 Good
 Average
 Poor



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Overview of the Russian tax system in 2013 and forecast for 2014



In crisis conditions for the global economy, Russia is not the only country to be paying particular attention to tax revenues. However, in contrast with other countries, the state decided not to introduce new taxes or to raise the rates of existing taxes. Instead, the priority was to abolish ineffective tax benefits and to make tax collection more efficient.

In the first half of 2014, Russia's Finance Ministry should complete its task of compiling a list of tax benefits, which it proposes to abolish. The new developments are already intended to be applied from 2015. Nevertheless, it is worth pointing out that the amendments will most likely affect those benefits with an uncertain effect on the economy. In Russia, the practice is to grant tax benefits, especially at a regional level, for major investment projects, when it is fully possible to calculate the macroeconomic advantages that the investment will generate. The amendments are highly unlikely to interfere here.

For now, the state is primarily focusing on tax collection. The tax authority has announced that the nature of tax audits will change. Whereas previously the practice was for scheduled tax audits of all taxpayers, now there will be much more frequent studies of the operations of very large companies,

which are capable of ensuring revenue for the state coffers (tentatively, there will be strenuous audits of the 20 percent of taxpayers who pay 80 percent of all taxes).

During tax audits, less attention is already being paid to matters of form (higher tax authorities often, when taxpayers appeal a tax office's decision, reject claims of a formal nature). Tax offices are attempting to identify unlawful tax evasion schemes and to get to grips with the purpose of entering into various transactions that on the surface seem unrelated and formally meet the conditions for tax benefits to be used: transactions with offshore companies, agreements to provide management services to foreign companies, royalties, loans and so on.

It is evident that many employees of tax offices that have major taxpayers on their books are increasingly qualified. Often during an audit, employees of the tax agency do not restrict themselves to documents that the taxpayers themselves hand over; instead, the auditors are using the internet to carry out their own detailed research of companies, are interrogating employees, and are exchanging information with other tax bodies, including some international ones. In 2014, the first tax audits can be expected under the transfer pricing law, which came into force in 2012.



By Anton Nikiforov

In line with the changing quality of tax audits, the tax authorities are also winning a higher number of the tax disputes that go to the state commercial courts. In Russia, as before, and regardless of the mandatory procedure that was brought in for a tax office's decision to be appealed to a higher tax authority, many disputes end up in the courts. Many companies have come to accept this as standard practice.

There are ever more disputes in which inspectors are accusing taxpayers of unlawful tax optimization. In this category of dispute, the court's discretion and the state commercial courts' subjective assessment of evidence are of considerable importance. This creates an unacceptable level of uncertainty in terms of the outcome of any dispute, which has to be solved.

The Russian Supreme State Commercial Court has put considerable effort into devising consistent approaches to resolving tax disputes. International conceptual approaches are applied in the area of tax and identifying unlawful tax evasion.

However, currently under examination are amendments proposed by the President to the Russian Constitution; these aim to abolish the Russian Supreme State Commercial Court and make the state commercial court system subordinate to the Russian Supreme Court (i.e. the highest court in the general, non-commercial court system). These amendments are very likely to be passed, which creates additional uncertainty for many taxpayers in calculating their taxes. The Supreme Court may take a different position, disagreeing with the Supreme State Commercial Court, in interpreting various issues of tax legislation.

As in many other countries, in Russia criminal liability and not just tax liability is stipulated if taxes are not paid in full. Some time ago practice

was substantially amended regarding a company's officers being held criminally liable. Police bodies may not conduct their own tax audits. They may only decide whether to initiate criminal prosecutions based on the materials that a tax office hands over to them after a tax audit is completed. Moreover, any prosecutions that are brought will be terminated if the taxpayer pays off its tax debt. As a result of this, the number of prosecutions is minimal.

However, a draft law is currently being examined, which would generally reinstate the old regime – irrespective of the outcome of tax audits, law enforcement bodies will be able to conduct their own investigations of tax crimes and bring prosecutions. In all probability, these amendments will be passed and will come into force in 2014.

This factor has a significant impact on the deadline for paying tax. Currently, taxpayers pay tax they owe, as a rule, once the court dispute is over (when it has gone through courts of three levels). After these amendments, to avoid criminal liability for their management, companies are likely first to pay the amount of tax, default interest and fines that is demanded, and then litigate to challenge the tax office's decision.

The events mentioned above occurring towards the end of 2013 will dictate the lines along which Russia's tax system will develop in 2014.

Anton Nikiforov is a partner at Peperliaev Group and practice in the areas of tax law and arbitration proceedings.

The GC Grapevine is now monthly and will be launching a new website shortly. Both the print and web editions will include a variety of new features as well as up-to-date news from around the globe that impacts both inside and outside counsel.

For more information on advertising in the new monthly GC Grapevine please contact

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