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An amendment transposing the 5th AML Directive enters into force in November

The 5th AML Directive introduces namely measures to increase the transparency of beneficial ownership, extends the scope of obliged entities to virtual currency service providers, strengthens the rules for the assessment and increased care of obliged entities for clients from high risk third countries and addresses the risks associated with anonymous prepaid instruments.

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Since 1 November 2020, the amendment to the Act No. 297/2008 Coll. on protection against money laundering and on protection against financing of terrorism comes into effect, transposing the 5th AML Directive into Slovak legislation. The key changes include:

1. Scope of obliged persons

Based on the development and experience from practice, the 5th AML Directive revises the scope of obligated persons listed in Section 5 of Act no. 297/2008.

Under Slovak law, the transposition of the 5th AML Directive implicates :

i) narrowing of the scope of obliged persons in the rental of real estate and art shops by introducing a criterion of the value of brokered business and setting the threshold to EUR 10 000,

ii) extension of the scope of obliged persons in the category of auditors, external accountants and tax advisors to include other persons who provide assistance in tax advice. Amendment to the Act no. 297/2020 also includes in this category other persons who provide advisory services in tax matters pursuant to special regulations, for example pursuant to the Act on Trade Licensing or the Act on Advocacy. Persons who undertake to provide, directly or through other persons with whom that other person is connected, material assistance, assistance or advice in tax matters as their principal business or professional activity should be included in the extended scope of the regulation.

2. Framework for virtual currencies

The approved amendment represents a major milestone in the provision of services related to virtual currencies.

Based on the amendment, the obligated persons will also include entities providing certain services related to virtual currencies as providers, that professionally deal with currency exchange services between virtual currency and uncovered currencies (fiat currencies), or virtual currency wallet service providers.

This means in practice that after the amendment, these providers will also be obliged to, for example, identify the client (KYC) and end user of benefits, find out information about the purpose and nature of the planned transaction, perform client control or report unusual transactions.

The amendment also introduces some new legal definitions of the related terms "*virtual currency*", "*virtual currency wallet service provider*" and "*virtual currency service provider*". The condition for the provision of both of these services will be the acquisition of a trade license for a licensed trade. For the sake of completeness, we add that a trade license issued for a trade whose content meets the characteristics of the provision of virtual currency exchange services or the provision of virtual currency wallet services issued before 31 October 2020 expires on 28 February 2021.

3. UBO data

The 5th AML Directive strengthens public access to beneficial ownership information in relation to the public availability of data on ultimate beneficial owner (UBO). The changes to the 5th AML Directive also include the strengthening of the exchange of information on UBO's and the introduction of a central register of UBO.

The most significant change in the current regime of data publicity is that the new data on a UBO will be publicly available to the following extent: name, surname, date of birth, nationality and address of residence, as well as data establishing the status of UBO.

The amendment responds to this request of the 5th AML Directive in such a way that the function of the central register of UBO will be provided by the Register of Legal Entities, while the above-mentioned data on UBO should be available to the general public from 10 January 2021. This data is to be provided by the Statistical Office of the Slovak Republic through its website, and the data made available in this way would be free of charge.

4. Additional changes

The 5th AML Directive expressly provides that, when implementing due diligence measures, equivalent requirements will apply to legal entities such as foundations and legal structures similar to the management of entrusted assets.

The amendment therefore requires that when obliged persons enter into a business relationship not only with a business undertaking but also with an entity with a similar legal structure (e.g. a foundation, a non-profit organization providing services of general interest, a non-investment fund or other special purpose vehicle) they must require a certificate of registration or an extract from the relevant register and the identification of the individual who is authorized to act on its behalf.

The amendment also establishes a cross-reference to the Notarial Code by explicitly stipulating that the fulfillment of notaries' duties under Act no. 297/2008 is not limited by the statutory obligation to maintain confidentiality under the Notarial Code. The change responds to practice, according to which in the past notaries refused to provide the financial intelligence unit with the necessary co-operation during the inspection due to the statutory obligation to maintain confidentiality in the Notarial Code.

The amendment also furthers the scope of politically exposed persons by persons of national or regional significance, on the basis of which, for example, representatives of municipalities or officials of the prosecution.

Case law

The Court of Justice of the European Union ruled in Slovak VAT case

The Court of Justice of the EU issued order in case C-621/19 Finančné riaditeľstvo Slovenskej republiky v Weindel Logistik Service SR spol. s r.o. which deals with the possibility to claim import VAT deduction by the importer who does not become the owner of imported goods.

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The Company Weindel Logistik Service SR spol. s r.o. (hereinafter „WLS“) provides repacking services. During 2008 imported to Slovakia goods for repacking with the origin in Switzerland, Hong Kong and China and paid import VAT that was claimed as input VAT deduction. Repacking service was charged to Swiss customer who remained the owner of these goods during the whole time. After repacking the goods were supplied in another EU Member States or exported to third countries.

The Tax Authorities challenged input VAT deduction claimed by WLS arguing that WLS:

- was not the owner of the imported goods,
- did not incur any costs that could be reflected in the price of output taxable supplies,
- did not use imported goods for its economic activity as taxable person.

WLS objected that without importation of the goods it could not provide services and should the input VAT deduction be possible only if the price of the goods was booked as a cost, this condition could not be fulfilled.

The Court of Justice of the EU confirmed the opinion of the Tax Authorities and ruled that **the right for input VAT deduction would not be granted to the importer if:**

- **he does not dispose of the goods as their owner and**
- **the importation costs have not incurred on the input side or are not included in the price of the outputs or in the price of the goods and services supplied by the taxable person within his economic activity.**

Should you be interested in VAT advisory services with respect to any transactions performed, please contact us.

Case law

The Court of Justice of the EU decided on the deduction of input VAT for construction work on public roads carried out free of charge for the benefit of a municipality

On 16 September 2020, the Court of Justice of the European Union ("CJEU") released its judgment in the case C-528/19 „Mitteldeutsche Hartstein Industrie AG". CJEU dealt with questions whether it is allowed to deduct input VAT related to construction work carried out on a public road for the benefit of a municipality and whether extension of a public road completed free of charge for the benefit of a municipality represents a supply of goods for consideration.

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The Case

The managing holding company Mitteldeutsche Hartstein-Industrie AG forms a tax entity with its subsidiaries, A GmbH ("A") and B GmbH ("B").

The company A was authorised by a regional administration to reopen and operate a limestone quarry. Granting of the authorisation was subject to the development of access to it by way of a public road belonging to the municipality. The company A agreed to bear all of the costs relating to the extension of that road and the municipality promised to make the extended road available to A to be used, inter alia, by its heavy goods vehicles without restriction, if it remained open to the public. The company B was commissioned to carry out that extension.

The input VAT from the received goods and services related to completion of construction work by the company B was claimed via the filed VAT return. The costs incurred by A GmbH for the works for the extension of the municipal road in question were not taken into account.

The tax authorities held the view that by constructing the extension to the municipal road in question, the respective company had provided the municipality concerned with free-of-charge work subject to VAT and therefore, adjusted its liability accordingly.

CJEU dealt with the following questions:

1. Is a taxable person entitled to deduct input VAT paid for works for the extension of a public road carried out for the benefit of a municipality?

- CJEU mentioned that without the works for the extension of the municipal road in question, it would have been

impossible to operate the limestone quarry, from both a practical and legal point of view. It follows from the circumstances of the case at hand that the works for the extension of the municipal road in question were essential in order for the operation of the limestone quarry to come to fruition and that, without those works, the company would not have been able to carry out its economic activity.

- The fact that the public may use the municipal road in question free of charge is, according to CJEU, immaterial. The works for the extension of that road were carried out not for the purposes of the municipality concerned or of public traffic but in order to adapt the municipal road in question to the heavy goods traffic generated by the operation of the limestone quarry by the company.
- **If the works for the extension of that road were limited to what was necessary for the mentioned purposes, the right to deduct should be recognised for all the costs resulting from those works, in so far the costs of those works are included in the price of the output transactions carried out by that taxable person.**
- **By contrast, if those works exceeded what was necessary to ensure the operation of that quarry, the right to deduct would have to be recognised only for the input VAT levied on that portion of the costs that was incurred for the works for the extension of the municipal road in question which was objectively necessary to allow the respective company to carry out its economic activity.**

2. Does the authorisation to operate a quarry constitute consideration received by a taxable person which carried out, without monetary consideration, works for the extension of a municipal road?

- The authorisation to operate the quarry was an unilateral decision taken by the regional administration. However, it follows from the case-law of CJEU that a unilateral act by a public authority cannot, in principle, impose a legal relationship entailing reciprocal performance.
- **Granting this authorisation therefore does not constitute consideration received by a taxable person which carried out, without monetary consideration, works for the extension of a road belonging to a municipality. Those works thus do not constitute a transaction carried out for consideration.**

3. Do the works for the extension of a public road carried out, free of charge, by a taxable person for the benefit of a municipality constitute a supply of goods made for consideration?

- CJEU stressed that the purpose of the provision under which certain transactions for which no real consideration is received by the taxable person are treated as supplies of goods effected for consideration and subject to VAT, is to prevent situations in which final consumption is untaxed.
- Even though the municipal road in question is open to public traffic, the actual end-use of that road should be, according to CJEU, taken into consideration.
- The mentioned company benefits from the works for the extension of that road. They have a direct and immediate link with its overall economic activity which gives rise to taxable transactions. The costs of the input services received and linked to the works for the extension of that road form part of the factors in the cost of the output transactions carried out by the company.
- **The works carried out, for the benefit of a municipality, for the extension of a municipal road open to the public but used, in connection with its economic activity, by the taxable person which carried out those works free of charge and by the public, do not constitute a supply of goods made for consideration.**

Depending on factual and legal circumstances of each individual case, this judgement may have a favourable impact on VAT treatment of induced investments related to projects of developers, as well as in cases of work carried out without consideration on other person's property, or services used, in addition to the taxable person, by third parties.

Case law

Transfer pricing adjustments can lead to tax risks

The Municipal Court in Prague confirmed the approach of the Tax Authorities who reclassified marketing services contractually rendered abroad to the consideration received from a third party that should be included in the tax base for local supply of goods and be subject to the Czech VAT.

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The Czech drug distributor sold drugs in the Czech Republic and Slovakia. He also invoiced marketing services to his Swiss drug supplier. Due to the price regulation, the purchase price of drugs bought from a Swiss supplier was higher than their subsequent sale price in the Czech market.

In the course of a tax audit that was focused on transfer pricing, the distributor claimed that the carried-out marketing activities represented an inseparable part of the drugs distribution. Following that, during the VAT tax audit, the Tax Authorities considered marketing services as an ancillary supply to the main supply which is the sale of goods. The Tax Authorities further claimed that marketing services are provided directly to the final buyers of drugs.

The court stated that due to the drug price regulation the distributor could not demand payment of a price that includes all its components (including marketing), and therefore the marketing activity was reimbursed by the Swiss supplier. The Tax Authorities thus reclassified the service with the place of supply in Switzerland to the consideration received from a third party for goods supplied in the Czech Republic, which is subject to the Czech VAT.

The court also considered the whole business model to be artificially created and application of other (more advantageous) tax regime for part of the consideration as incorrect.

The case will now be dealt with the Supreme Administrative Court, as this is a judgment of the Municipal Court in Prague.

Please contact us should you wish to discuss whether your business model contains similar risks.

EU list of non-cooperative jurisdictions for tax purposes was again revised

ECOFIN adopted a revised EU list of non-cooperative jurisdictions for tax purposes (the EU blacklist). The EU Finance Ministers agreed to add two new jurisdictions to the list as well as to remove two jurisdictions from the list.

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On October 6, 2020, ECOFIN adopted a revised EU list of non-cooperative jurisdictions for tax purposes (the EU blacklist). The EU Finance Ministers agreed to add two new jurisdictions to the list: Anguilla and Barbados, as well as to remove the Cayman Islands and Oman from the EU blacklist.

Following this latest revision, the EU blacklist includes twelve jurisdictions.

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