

EXPECTED CHANGES IN TAX LEGISLATION FOR 2010

Draft amendments to the tax legislation for 2010 were published on 7 October 2009. Most of the amendments are expected to enter into force from 1 January 2010. Still though there are some amendments that are proposed to enter into force retroactively (since 1 January 2009). It has to be taken into account that the published versions are only drafts and that the final versions adopted by the Parliament may be partly different.

Please find below a brief analysis of the most important draft amendments that could affect businesses and individuals.

VAT

Place of supply of services

The main changes are related to the change of the rules for place of supply of services. The general rule for place of supply of services will be that the services shall have their place of supply in the country where the customer is established, given that this customer is a taxable person. On the other hand, the general rule for place of supply of services to non-taxable persons (in most cases individuals) would determine the place of supply of services in the country where the supplier is established.

The rules for determining the place of supply of the following services remain unchanged (given that the transaction is between two taxable persons):

- services related to real estate;
- transportation services;
- services performed by intermediaries;
- sports, culture, entertainment, educational services,
- expertise, evaluation and work on movable goods;

The above draft changes are based on the changes in Council Directive 2006/112/EC that have to be transposed in the national legislation of each EU member state not later than 1 January 2010.

Practically, major part of the services (other than the specific exceptions provided in the law) rendered between companies established in two different countries would be subject to reverse charge VAT by the customer. On the one hand this would lead to fewer VAT invoices issued to foreign companies. On the other hand in case of tax audits it is possible that the revenue authorities split some services by elements and claim taxation by the supplier in Bulgaria if the services include costs on entertainment, restaurants, education, culture, etc.

Deadlines for deduction of input VAT are extended

Deduction of input VAT will be possible within 12 months after the date of the chargeability of tax. At present this deadline is three months after the date of the chargeability of tax. This amendment (if adopted) would have a positive effect on solving the practical issues arising from the delayed receipt of purchase invoices.

Taxable base for barter transactions

In case of barter transactions the taxable base will be the market price of the goods/services received as remuneration for the supply. Until present the taxable base for barter transactions was determined as the market price of the goods/services supplied.

Cash register devices

It has been proposed that all companies using cash register devices shall ensure distant connection of these devices with the National Revenue Agency and shall report their sales to the revenue authorities on a daily basis. For this purpose companies shall upgrade technically their cash register devices.

Other changes

The rest of the changes that might be important to the business are:

- a/ Obligation to register for VAT in case of supplying/receiving reverse charge services before performing/receiving the first transaction. This obligation would affect companies that are not registered for VAT yet (incl. newly established companies);
- b/ VAT on taxable supplies with continuous performance would have to be charged at least once per year;
- c/ The revenue authorities would be able to register for Bulgarian VAT purposes a foreign person that has not assigned a tax representative. This is valid only when the registration is initiated by the revenue authorities;
- d/ The first name and the family name of the individual who prepares invoices on behalf of the company would no longer be an obligatory requisite.

Expected changes in the procedures for refund of VAT paid in other EU member states

The refund claim will be submitted via electronic portal in Bulgaria maintained by the Bulgarian revenue authorities. The refund claim will be forwarded to the member state(s) in which the VAT was paid. One refund claim can cover VAT paid in several member states.

Deadline for submission of the refund claim is 30 September of the year following the year in which the VAT was charged. Deadline for refund is 4 months, but it could be extended to 8 months if

additional information is requested from the taxpayer, the Bulgarian revenue authorities or other institutions.

The additional correspondence between the taxpayer and the authorities of other member states will be via electronic means. The eventual appeal process against a rejected refund would be determined by the laws of the member state(s) in which the VAT was paid.

On the one hand these changes will make the submission of the refund claim much more standard and accessible to more taxpayers. At present this is a relatively slow and expensive process usually involving the assignment of agents or consultants in other member states.

However, in the case of disputes the taxpayer may still need to assign lawyers/consultants in the member state, in which the VAT was paid.

Withholding taxes

Tax base for withholding tax purposes

Currently, withholding tax is due on the gross amount of certain types of income. According to the European Commission, this is a discrimination of the EU residents compared to Bulgarian residents who are allowed to certain deductions on similar types of income.

According to the draft law amendments, the residents of EU/EEA (both legal entities and individuals) that receive income subject to withholding tax shall be entitled to opt for net tax base equal to the one allowed to Bulgarian residents, subject to certain conditions provided for in the law. This option may be exercised after the withholding tax calculated on gross basis is remitted to the state budget, where a refund claim may be filed along with an annual tax return. Details shall be further clarified (such as format of the tax return, contents, proofs for expenses to be required, necessity of financial statements to be prepared, etc.). In the case of non-resident individuals, the option is to be exercised through submission of the annual personal income tax return applicable for tax resident individuals.

Non-residents may face practical difficulties in applying this option.

Dividends

Dividends distributed to EU/EEA shall not be exempt from withholding tax in case of hidden distribution of profit. The definition of 'hidden distribution' is broadened.

Corporate Income Tax

Annual Tax Return

According to the now effective Corporate Income Taxation act (CITA), the audited financial statements shall be attached to the CIT annual tax return submitted by 31 March of the following year. Should the audit of the financial statements continue after that date, the audited financial statements shall be submitted additionally by 30 June of the following year. CITA allows also the submission of corrective tax return by 30 June of the following year in case of difference between the initially submitted and the audited financial statements.

The draft law amendments change this procedure. Companies shall not submit their financial statements to the revenue authorities but annual financial reports (on a standard form) submitted for statistical purposes. The draft leaves open several questions the most important one being the possibility to submit a corrective tax return corresponding to the figures in the audited financial statements. The new reporting rules are proposed to become applicable for the 2009 tax return and financial reports prepared for the current year.

Financial Institutions

The effective CITA does not contain provisions regulating the reversal of temporary differences in cases when a company has become a financial institution after those timing differences have arisen. The 2010 draft contains provision (new para 2 to art. 96), which purpose is to clarify that the income and expenses from subsequent revaluation of financial assets and liabilities that have not been recognized for tax purposes in previous periods shall be reversed applying the general rules and not the specific treatments applicable to financial institutions.

Income excluded from taxable base

According to the provision of art. 27 of the effective CITA income related to non-deductible expenses described in art. 26 CITA (permanent differences) shall be excluded from the CIT base. The draft excludes from this rule the income related to expenses not related to economic activities, expenses not supported with documents, penalties and interest resulting from violation of legislation, donations and hidden profit distribution. This suggestion is reasoned with the aim to prevent fraud but it leads to double taxation (income is taxable and the corresponding expense is not deductible).

Individual Income Tax

New type of employment relation for tax purposes

According to the proposed amendments to the Individuals' Income Taxes Act, the relations with individuals-shareholders of limited liability companies (OOD) and holders of over 5% of the share capital of joint-stock companies (AD) will be deemed employment relations for tax purposes for the work performed by the individuals for the company.

Other changes

The income from sale (barter) of one residential immovable property will be tax exempt only if over 3 years have passed since the acquisition date.

It is stipulated expressly that taxable income will not be deemed to arise at the date of acquisition of shares in consideration of contributions in kind made to the capital of commercial companies.

In their annual personal income tax returns, individuals will be required to declare loans given/received/outstanding at a total of over BGN 5000 (other than credits provided by credit institutions).

Local Taxes

According to the draft amendments of the Local Taxes and Charges Act, the upper limits of the tax rates of certain local taxes (including real estate tax and transfer tax) are increased.

A liability for the payment of transfer tax will arise for real estates, limited property rights on real estates and motor vehicles, included in the assets of an enterprise, subject to transfer or transformation except for cases with change of the legal form.

The information in this material has as purpose only to note certain issues related to the expected changes in tax legislation for 2010 and is not exhaustive. Should any questions arise, please do not hesitate to contact us at tel.: 02/943 37 00, fax: 02/943 37 07, e-mail: office@afa.bg or at 38, Oborishte Str., Sofia 1504.