



SLOVAKIA

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Slovakia is known for its favourable geographical position in the heart of Europe and in spite of the negative effects of the international financial and economic crisis and despite a partial change in economic policy has been able to maintain its attractiveness to German investors. In particular this is thanks to membership of the European customs and currency union, growth which continues to be high in European terms, a relatively low level of taxation, well qualified and inexpensive workers and the well-developed infrastructure in the western part of the country. Higher taxes on company profits and the changed labour law has led to Slovakia losing some of its attractiveness for foreign investors, but Germany remains one of the most important trading partners of Slovakia with a number of large investors and also a large number of foreign medium-sized companies.

In spite of many common elements between the German and Slovakian legal systems there are also many differences, whereby in the following we would like to highlight just a number of interesting and useful peculiarities.

Thanks to the start-up of the central portal of the public authority (ÚPVS) in the internet (www.slovensko.sk) which enables uniform access to information and services of the public authority, the administrative process of the founding a company and the changes in the company which are subject to registration have along with other things been significantly simplified. The registration at this portal and the activation of an electronic key enable the registration at the commercial register and the trade licencing office directly from the company premises. The countersigned original documents no longer have to be presented in paper form, but are scanned in and sent via the portal to the authorities for processing.

As a result, since January 1, 2014 the registration application for the commercial register takes only two days to be authorised after presentation of all the required documents and allocation of the fee payment which is made by bank transfer. Furthermore, it remains possible to make applications in paper form. In Slovakia, Rödl & Partner for cost reasons also prefers to use the electronic form as in this case the fees at the commercial register are reduced by half and in the process at the trade licencing office in a number of cases are even cancelled.

In order to improve the quality of public services for citizens and companies, the law on electronic services from the public authority, the so-called eGovernment, came into effect on November 1, 2013. A component of eGovernment is also the obligatory setting up of an electronic letter box for public sector entities, legal entities and natural persons, entrepreneurs and subjects of international law which has to be activated in the course of 2015. Public sector bodies (including the tax and customs authorities) are then obliged to exercise their electronic public power and companies must also regularly check their electronic mail boxes as many

items will be sent to these mail boxes including summons, fines and if applicable other written documents from the authorities.

In Slovakian subsidiaries of German clients it is usual to grant discharge to the (in particular German) managing director. There is often dismay that the Slovakian legal system does not foresee a discharge of the managing director by the shareholders, whereby in fact discharge of liability in relation to possible claims for compensation on the side of the company are expressly forbidden. It is valid that the company can only dispense with claims for compensation after a period of three years as far as the shareholders' meeting agrees to this.

German clients sometimes assume that in the design of contracts claims for compensation can be excluded for some contract violations or that the damages can only be regulated for certain contract violations. A claim for compensation, however, is in principle only alterable by mutual consent if for certain contract violations a contract penalty has been agreed. Although a full exclusion of claims for compensation before the contract violation is not possible under Slovakian commercial law, but a part of case law allows certain limitation of indemnity for example through an upper limit or exclusion from certain types of damages as far as such a limitation does not bypass the law which prohibits the waiving of indemnity (e.g. a symbolic sum of money would not be permitted). To the extent that a contractual penalty was not agreed, the actual damage should not be fully excluded. In addition, it is valid that the court cannot reduce the loss incurred.

A German entrepreneur may be astonished to learn that in Slovakia since February 1, 2013 there are certain restrictions with regard to the agreement of due dates for receivables and in favour of the creditor. As far as monetary payment via instalments has not been agreed, the payment deadlines are in principle not longer than 60 days after the invoice has been sent or after the day of the performance of the creditor. The parties can only agree to a longer period for payment as far as such an agreement is not in major disproportion to the rights and obligations of the contractual obligations of the creditor with regard to interest on arrears. If an investigation after the performance of the creditor is to be carried out in order to determine whether the creditor has performed properly, the time period for fulfilment of the payment obligation of the debtor begins on the day after the conclusion of the investigation which has determined that the performance has been correctly carried out.

The agreement of a time period longer than 30 days required for the investigation after performance is allowed provided it is not in major disproportion to the rights and obligations of the contractual obligations of the creditor with regard to interest on arrears. This provision is mandatory and cannot be contractually excluded.

In Slovakia it is advisable to be particularly alert when purchasing real estate. We know from experience that it can constitute a risk to exclusively rely on the registrations included in the land register as is often the case with entrepreneurs, whereby later it may come to light that the property was acquired from a person who was not the owner. Double ownership is a typical phenomenon as a result of incorrect or missing proof of the acquisition of real estate during the socialist government of the past. Although the principle of trust remains valid in Slovakia (i.e. the registrations in the land register are worthy of trust unless proven otherwise), it is often the case that after the acquisition of a property a third person raises claims against the acquiring party (e.g. for inheritance reasons in connection with a former owner if the property was still listed under lot numbers in a historical registration (prior to the change of the land register system) or due to acquisition in a process according to the restitution laws which are conducted by a separate office (state land office) and are not visible in the land register). It may also transpire that the property is the subject of legal proceedings. If an acquisition of real estate is planned a complex examination of the relationships is definitely recommendable in order to discover possible risks.

In connection with the legal relationships relating to the rental of commercial space we repeatedly encounter the problem that the notice of termination for commercial premises with a fixed term is only possible according to legally permissible grounds which according to the predominant view are final, i.e. not extendible by contract or cannot even be changed by mutual consent. Accordingly, an extension of the grounds for annulment must be formulated as a cancellation of the contract, otherwise the parties are exposed to the risk that in the event of a dispute the extension of the contract grounds would not be recognised by a court of law. In addition, an entrepreneur has to assume that even if the legal grounds for termination are not included in the contract or are excluded, these will find application by law.

A further problem for the entrepreneur operating in the area of real estate is the fact that although with the disposal of a property the new owner takes the legal position of the former landlord, the tenant is entitled by law to terminate the rental contract within the period of notice to the next possible date of termination. The exercise of this right cannot be avoided by mutual consent in a contract and also cannot be punished by a contract penalty, whereby the waiving of this right is only possible after the tenant has changed. Accordingly, in connection with the disposal of properties which serve to generate rental income, such a waiver has to be fixed to be at the earliest on the day of the effectiveness of the sale.

Slovakian labour law has been mainly harmonised and the differences to German law are not serious. In connection with employment relationships, however, German companies are still not used to the exploitation of the institute of the workers' representatives in order to increase work efficiency and ultimately to reduce costs. Only with the participation of the workers'

representatives can the employer influence the introduced working time to any degree, e.g. the introduction of flexible time accounts, lower wage replacement for work restrictions on the side of the employer (e.g. lack of work).

In the course of exercising their activities in Slovakia, German entrepreneurs should take into account that in Slovakia the institute of liability for sales tax at the preceding sales tax level was introduced with effect from October 1, 2012. The customer (taxpayer) is liable for the sales tax (output tax) from the preceding sales level which is listed in the invoice of the supplier if the supplier does not pay the output tax or is unable to pay the output tax and the customer at the time when the tax liability was created should have due to reasonable grounds known or could have known that the tax would not be paid.

The sales tax law explicitly specifies which facts can be assessed to be reasonable grounds such as when the equivalent value for the performance is excessively high or low without economic justification, when the customer at the time when the tax liability is created is personally connected to the supplier by means of a legal entity or a shareholder, or when the customer has continued the transactions with a taxpayer where the grounds to cancel the registration have occurred and he has been published in a blacklist (list of persons maintained by the financial department of the Slovakian Republic). Reasons for the cancellation of the registration are, for example, if the company in the calendar year is repeatedly unable to fulfil its obligation to submit a tax return, if the company has repeatedly not paid its tax liability, or if the company is repeatedly not available at the domicile of the company.

As from January 1, 2014 sales tax payers have a further obligation to submit a so-called control report for the respective assessment period in addition to the tax return and the summary report which they already have to submit. This control report must include details about the tax obligation and input tax deduction and must be submitted exclusively using electronic means. This measure represents a further financial and administrative burden to taxpayers who use foreign financial accounting software without a module which supports the export of the control report in XML format.

The financial accounting standards in Slovakia are slowly being adjusted to the IFRS standard. IFRS does not define an exact system of accounts or structure of the annual financial statement. Despite the implementation in stages of IFRS elements in the Slovakian financial accounting there remain differences between the local financial accounting regulations and international standards. In contrast to international standards (IFRS) and the standard which prevails in Germany (HGB), the Slovakian regulations exactly define the system of accounts, the content of the individual accounts, the structure of the balance sheet, the income statement and the notes to the annual financial statement. This fact is often ignored by German investors

when they enter the Slovakian market especially with the introduction of standardised software which also includes the area of financial accounting and controlling. At some later date the company then has to adapt its software to the financial accounting requirements in Slovakia which is associated with not inconsiderable costs.

Practical examples

Auditing

Background facts:

A German manufacturer of components for the automotive industry does business in Slovakia with its 100 %-owned subsidiary. The parent company manages the strategic purchasing, marketing, logistics, development, controlling and IT for its production company in Slovakia. The company has decided to introduce standardised software to the whole company group which will also include the financial accounting. The company thereby plans to improve the efficiency of individual areas of the operational management, including the financial accounting. In the ordering process of the software in co-operation with the software supplier, the company included its own requirements for the management of the departments listed above and for the applicable regulations for financial accounting and preparation of the annual financial statement valid in Germany. The chart of accounts was set up to meet the requirements of the German commercial code with respect to financial accounting and the preparation of the annual financial statement. A system set up in the same way was introduced to the subsidiary in Slovakia. After the time-consuming and costly installation of the software the auditor of the subsidiary determines that the chart of accounts, the balance sheet and the income statement do not correspond to the applicable regulations in Slovakia. In contrast to the German commercial code, the Slovakian law governing financial accounting exactly defines the chart of accounts and structure of the balance sheet, the income statement and the notes to the annual financial statement.

What can be done now?

In order to make the software conform to the applicable regulations in Slovakia, the company has to contact the software supplier. The adjustment of the software to conform to the applicable regulations for financial accounting in Slovakia will, however, involve further costs.

What should one have done differently from the beginning?

The company could have discussed the adjustment of the software with regard to financial accounting with the advisors from Rödl & Partner already at the stage of placing the order to the software supplier. Then the complete course of the implementation of the new software would have been more efficient and with much lower costs.

Taxes

Background facts:

A German company with operations in the chemicals industry has decided to found their subsidiary X in Slovakia. In the course of company activities company X also concludes a number of contracts with Slovakian suppliers. One of the suppliers of company X was also company Y where pursuant to the Slovakian sales tax law grounds to cancel the registration occurred. Such grounds primarily include facts whereby the company during the calendar year has repeatedly not fulfilled its obligation to submit a tax return, has repeatedly not paid its tax liability or was not available at its domicile. The financial authorities of the Slovakian Republic placed company Y on the list of companies where grounds for cancellation of the registration have occurred, i.e. on a blacklist, and published this list on the web portal of the financial authorities.

Due to the fact that company X did not check its supplier, company X also continued with the execution of taxable business with company Y, although this company was already included in the publicly available blacklist.

In this case both conditions for the enforcement for liability for tax from the preceding sales level were satisfied, i.e. the supplier did not pay the tax office any output tax and at the same time the customer should or could have known that the tax from goods delivered to him in the domestic market is not paid. For this reason in an official notification the tax office ordered company X to pay the outstanding tax. Company X had to pay the tax amount listed in the notification within eight days to the tax office. The contract with company Y did not include a regulation for such cases and, if at all, company X is at the most left with the possibility of claiming compensation from company Y. As the case concerned a large order, the liability for tax from the preceding sales level had a considerable negative effect on the operations of company X.

What can be done now?

It is possible for company X to lodge an appeal against such a decision of the tax office within eight days after the notification is sent. Due to the fact, however, that the conditions of the institute for tax liability have been fulfilled, the appeal filed will most likely not be successful.

What should one have done differently from the beginning?

If company X when entering into business relations with a Slovakian supplier had taken expert advice at the beginning, it would have mostly avoided the respective inconvenience. Rödl &

Partner can help with checking the companies in the blacklist or with the drawing up of the contract conditions in order to minimise the financial risk from liability for tax from the preceding sales level.

Taxes

Background facts:

The German citizen and tax resident, Mr. Günther, has decided to engage in entrepreneurial activity in Slovakia with a newly founded company with limited liability (s.r.o.) and became the sole shareholder of this company.

The profit recorded by his company (s.r.o.) for 2013 was subject to the Slovakian corporation tax of 23 %. The profit share (dividends) which Mr. Günther subsequently distributed were not subject to further taxation in the Slovakian Republic as the shares distributed from profits realised after January 1, 2004 to persons with an interest in the assets of the distributing company are not subject to income tax. Mr. Günther then subsequently, as a citizen and especially as a tax resident in Germany, submitted his world income tax return in Germany in which as well as other income he also declared the distributed profits (dividends) from the area of Slovakia. As this profit share (dividends) was not subject to tax in the area of Slovakia, it was taxed in Germany.

Although Mr. Günther was able to supply information confirming that the profit share (dividends) was not liable for income tax in the area of Slovakia, and for this reason had erroneously assumed that this fact would help him to reduce his tax burden, the opposite was true. In the end, due to his choice of the s.r.o. as company form in Slovakia, after the taxation in Germany Mr. Günther was left with less of the distributed dividends than he first thought.

What can be done now?

If Mr. Günther had sought advice from Rödl & Partner before the start of his company activities in Slovakia in order to minimise his tax burden and after that use his investment capital more efficiently, the tax consultants under consideration of the fact that profit shares (dividends) are not subject to tax would have been able to recommend a business model better suited to reduce the tax burden such as, for example, a limited partnership (k.s.) where Mr. Günther would have participated as a limited partner.

As the legal form of the limited partnership can be viewed as a partly transparent company, the profit share of the limited partner according to Slovakian law is taxed with the shareholder and the share of the limited partner with the company. The profit share (dividends) paid out to the limited partner (Mr. Günther) already represent the appropriation of the profit after tax (the profit was namely taxed through the k.s.). The profit share is not liable to any further taxation as the dividends according to the prevailing law do not represent an item subject to tax.

As these dividends were already taxed on a lower level (in the area of Slovakia through the k.s.), the double taxation in Germany can be avoided through citation of the method of exemption subject to progression which in practice means that the income from dividends in the tax return of Mr. Günther in Germany will indeed be included, but only for the purpose of determining the progressive tax rate according to which the rest of his income is taxed.

What should one have done differently from the beginning?

The application of a transparent company structure in the area of the Slovakian Republic (k.s.) would have allowed the total tax burden of Mr. Günther to be incomparably lower than in the case of a non-transparent structure (s.r.o.). If Mr. Günther had discussed the founding of a company in the area of the Slovakian Republic with Rödl & Partner in advance, he could have avoided the negative tax effects on his person and would have been in a position much earlier to enjoy the tax advantages from the application of a semi-transparent company structure in the area of the Slovakian Republic.

Law

Background facts:

The supplier, company X, and the customer, company Y, have concluded a contract to deliver and install a production line. In the event of a delivery delay a contractual penalty was agreed, whereby all claims for compensation above the contractual penalty are excluded. The plant was correctly delivered in time and accepted by the customer. After about half a year of operation of the production line a component fails, whereby the defect is only determined after the manufacture of a certain number of non-conforming products.

After the defect is discovered and until the repair can be carried out, company Y has to immediately stop operation of the production line and also production on further linked machines. Although company X managed to remove the defect through the delivery and installation of a new component, due to problems with the production and delivery of the

affected component, however, the complete process to remove the defect lasted nearly four weeks. The production line was connected to further production lines which therefore also had to stop operation. Finally, company Y asserted a claim for replacement of the damages incurred as a result of the stop in production, for the actual damage caused by the production of non conforming products, and for the lost profit for the time period when the production line and connected productions lines were out of operation. The defence of company X was that in the contract the right to compensation was excluded and that company Y should claim the contractual penalty for delayed performance.

The court ruled in favour of company Y and awarded the complete amount of damages claimed. The basis for the ruling was that the damages were only excluded in the case of delay of the work provided by the contractor (the contractual penalty was agreed for this case and not for any other case). However, damages were not excluded for other cases of violation of contractual obligations (in this case with the removal of a defect within the scope of the guarantee) with reference to the legal regulation that the claims for damages arising from the infringement of contractual obligations cannot be waived.

What can be done now?

If the contract is concluded to be legally valid, in the case of a dispute the court can only rule within the framework of the law and the agreed regulations. After the event it is unfortunately not possible to reverse the facts. In order to pre-empt a legal dispute, clear and appropriate regulations must be determined before the conclusion of the contract.

What should one have done differently from the beginning?

Prior to conclusion of the respective business the company should seek expert legal advice. Although under Slovakian commercial law complete exclusion from claims for compensation prior to infringement of the contract is not possible, it is permissible to limit such claims to a certain extent in advance, e.g. through a contractual penalty, through the exclusion of consequential damages or loss of profit, or through introduction of a reasonable upper limit. With the support of Rödl & Partner the contract can be adapted to take the particularities of Slovakian law into account and to adapt to the case in question and as in this case to clearly and definitively agree the claims for compensation in order to avoid the situation that the client is faced with an unexpectedly large claim for compensation.

Fraud

Background facts:

Company X had a Slovakian managing director L who was entitled in the name of the company to act only in combination with a second managing director. The managing director and the company X have concluded a managing director's contract and also a contract of employment. The remuneration for employees should be authorised by a system introduced by the German shareholder. Due to dissatisfaction with the managing director the German shareholder dismissed the Slovakian managing director and now also wanted to end the employment relationship. The managing director drew up a supplement to his employment contract (backdated for the time period of exercising the function of managing director) immediately without obtaining the signature of the second managing director according to which he was entitled to a disproportionately high rate of remuneration compared to the previous amount of remuneration and immediately himself instructed the payment of the remuneration.

The German shareholder only later established that the remuneration was made without authority and therefore it was deducted from the next remuneration of L to the extent that L according to the opinion of the shareholder did not have a right. The managing director filed a suit against company X for the unauthorised deduction of the money. The court ruled in favour of the managing director and the company was obliged to repay the managing director even though the manner of acquiring the remuneration was fraudulent.

In its decision, the court did not assess the entitlement of the remuneration payment, but only the formal error which company X had made that with an employment relationship a one sided deduction from wages is not permissible (only for legal reasons which in this case were not present). In this case a deduction from wages would be possible due to a mutual written agreement which, however, had not taken place.

What can be done now?

The company can retroactively file suit against the managing director to realise repayment on grounds of unjust enrichment and apply for repayment of the unauthorised paid out remuneration and if applicable introduce criminal charges against the managing director on the suspicion that a fraudulent act has been committed. However, the costs incurred for the previous legal action, will not be reimbursed by L.

What should one have done differently from the beginning?

After irregularities are determined in the financial accounting, company X should have immediately contacted Rödl & Partner. Rödl & Partner would propose a suitable course of action to correct the named irregularities. In this case one could demand the conclusion of an agreement regarding deduction from wages and with a negative attitude of the managing director company X was able to take legal action regarding unjust enrichment.

Corporate (white-collar) crime

Background facts:

Company X has 100 employees. On the day when the wages are due company X has the financial funds available to pay the wages. The majority shareholder of company X is the German company Y, whereby the managing director of both companies is Mr. Jan. Shortly before the wages are due for payment in company X, however, company Y must also cover its liabilities, whereby the company does not have an adequate cash flow and the delay of company Y with the payment of its liabilities would be associated with high penalties. Due to the fact that in the past company Y had granted a loan to company X, Mr. Jan considers the possibility that company X could pay back the loan to company Y and that this would eliminate the risk of high penalties.

Mr. Jan has also taken the fact into account that company X recorded outstanding debts against its customers and assumed that these debts would be paid in a few days to company X. Due to this assumption Jan decided that the wages due for payment would be paid after receipt of the money paid by the customers of company X (i.e. not on the day when the wages were due, but with the assumed delay of a few days) and that he would pay back the granted loan to company Y. He then acted accordingly, i.e. one day after the wages were due for payment company X transferred the funds to company Y.

Although company Y had eliminated the risk of high penalties, the further assumption of Jan, however, did not come to pass that the customers of company X would settle their liabilities. The wages in company X therefore remained unpaid.

What can be done now?

The situation which has occurred must be dealt with immediately. The lawyers at Rödl & Partner are able to assess the danger of the respective circumstances and propose solutions.

The non-payment of wages can namely be viewed as a criminal offence, whereby the danger of recourse in particular is borne by the legal entity, which in our case is Mr. Jan.

In general it is valid that in each individual case it is necessary to immediately assess the facts (for example, if the company urgently requires funds to maintain its activity) and act accordingly in respect of the situation. Under certain circumstances, company X could namely “prefer” other payments instead of wages or also an additional wage payment could as a result remove the liability of a criminal offence.

What should one have done differently from the beginning?

Company X or Mr. Jan should have and were obliged to continually monitor and assess the financial situation of the company. In the case of any indication whatsoever of impending financial problems or a lack of cash flow Rödl & Partner recommends taking actions with extreme caution and to discuss the facts of the case with experts beforehand. Measures to reduce the risk of criminal law penalties, for example, in the case of non-payment of wages, always depend on the actual situation and the state of the company. The bad financial situation of the company may indeed be just of a temporary nature or may show signs of insolvency in the sense of the bankruptcy law. In the event the company is bankrupt (whether in the form of illiquidity or over-indebtedness) it is even more important to proceed with caution because in this situation the action of any payment whatsoever (including wages, taxes, contributions) represents a risk and can qualify as a criminal offence in terms of fraudulent preference.