SLOVAK REPUBLIC

OUTLINE

LIST OF ABBREVIATIONS

Agreement	Agreement between the European Community and the Swiss Confederation providing for measures equivalent to those laid down in Council Directive 2003/48/EC on taxation of savings income in the form of interest payments
Directive	Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payment made between associated companies of different Member States
C.L.	Collection of Laws (equivalent of the Official Bulletin)
Merger Directive	Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States
OECD	Organization for Economic Cooperation and Development
OECD MC	OECD Model Tax Convention 2003
Parent-Subsidiary Directive	Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States
Savings Directive	Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments
ZDP	*Zakon o dani z prijmov* (Income Tax Act)
ZSDP	*Zakon o sprave dani a poplatkov* (Tax Administration Act)

LIST OF LEGAL REFERENCES

- Amendment No. 659/2004 C.L. to the Income Tax Act No. 595/2003 C.L.
- Income Tax Law, 595/2003 (Zákon o dani z príjmov).
- Tax Administration Act, 511/1992 (Zákon o správe daní a poplatkov).

PART I. IMPLEMENTATION OF THE DIRECTIVE

1. INTRODUCTION

1.1. GENERAL INFORMATION ON THE IMPLEMENTATION OF THE DIRECTIVE

The Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payment made between associated companies of different Member States (the "Directive"), as amended, was implemented into the Slovak legislation by the amendment No. 659/2004 C.L. to the Income Tax Act No. 595/2003 C.L. The provisions relevant to taxation of interest became effective only as of 1 January 2005 instead of 1 May 2004, the date of the accession of the Slovak Republic to the EU, whereas the provisions relevant to the taxation of royalties shall become effective as of 1 May 2006.

The following table shows the relevant sections of the amended Income Tax Act implementing the Directive.

Articles of the Directive	Relevant sections of the Income Tax Act
Art.1	13 (2) g), i) 2 t)
Art. 2	13 (2) g) 16 (1) e)
Art. 3	2 t) 13 (2) g), i) 16 (2)
Art. 4	-
Art.5 (1) and (2)	-
Art.7	-

1.2. TAX TREATMENT OF INTEREST AND ROYALTY PAYMENTS UNDER GENERAL TAX LAW

1.2.1. Domestic rules

a. Outbound interest and royalty

Interest and royalty payments are deductible for tax purposes. The deductibility of both types of payments is subject to the general transfer pricing provisions.

Interest

Interest on loans and credits, deposits on bank accounts, proceeds from bonds, deposit certificates, treasury bills and similar securities and investment instruments, paid by Slovak resident companies and Slovak permanent establishments of non-resident companies is a Slovak-source income subject to 19% tax withheld at source (ZDP section 43). This rate can be reduced by relevant double taxation treaties; in that case the reduction is applied at source. The withholding tax may, however, be eliminated or reduced under the terms of any relevant tax treaty.

There are no thin-capitalization rules.

Royalty

Royalties paid by Slovak resident companies and Slovak permanent establishments of non-resident companies are Slovak-source income subject to a withholding tax at a 19% rate (ZDP section 43). This rate can be reduced or eliminated under a tax treaty.

Payments for the use or right to use certain movable assets located in the territory of the Slovak Republic (rental payments) are also treated as Slovak source income. Special tax treatment applies to these payments. The Slovak company paying rental payments to a non-resident entity is obliged to withhold a collateral tax in the amount of 19% (ZDP section 44). The collateral tax serves as an advance payment of tax and can be deducted against the final tax liability in the tax return filed by a non-resident taxpayer. When filing the tax return, a non-resident may also apply the tax rate for royalties as per individual double taxation treaty.

b. Inbound interest and royalty payments

Interest or royalty income derived by resident companies is generally included in the taxable income and subject to general corporate income tax rate.

Any foreign withholding tax rate levied on the inbound interest or royalties may be credited against the Slovak tax liability only in the case, where the applicable tax treaty provides so. No unilateral double taxation relief is available.

c. Transfer pricing

If the agreed price for a transaction is different from the fair market price and the difference cannot be satisfactorily explained, the fair market price will be substituted for tax purposes. Transfer pricing rules apply to transactions between economically or personally related persons. Related persons are generally defined as persons who participate directly or indirectly in the management, control or capital of the other person. Special transfer pricing rules exist regarding permanent establishments of non-residents. It should be noted that from 1 January 2004 transfer pricing rules do not apply between resident related parties.

1.2.2. Treaties

The Slovak Republic has tax treaties with all the EU Member States, except Estonia, which still needs be ratified (see Annex).

In the absence of unilateral double taxation relief the tax treaties remain important as they make the relief of double taxation possible. For relief of double taxation in respect of interest and royalty payments usually the credit method is being followed. This is particular relevant in the bilateral relations with countries benefiting from the transitional period on interest or royalty payments.

a. Interest

It is a general tax treaty negotiation policy of the Slovak Republic to provide for the exclusive taxation of interest in the state of residence. Currently, most Slovak tax treaties with EU Member States provide for exemption from withholding tax on interest in the source state.

However, the tax treaties with Belgium, Cyprus, Greece, Latvia, Lithuania and Poland provide for a 10% withholding tax in the source state and the tax treaty with Portugal for 15% withholding tax.

b. Royalties

It is a tax treaty negotiation policy of the Slovak Republic to provide for a limited taxation in the state of source of the royalty payments. Usually a treaty will allow a 10% withholding tax to be imposed on the gross amount of royalties in the source state.
In some treaties, an exemption from taxation in the source state is provided for the cultural royalties (for the right to use or use of copyrights or literary, artistic or scientific work, including cinematograph films).

Most of the double taxation treaties concluded by the Slovak Republic (with certain exceptions, as for example the treaties with Ireland, Malta and the new treaty with Belgium) include payments for the use of, or the right to use, industrial, commercial or scientific equipment in the definition of royalties.

2. SCOPE

2.1. PAYMENTS

2.1.1. Concept of interest

a. Definition

The term "interest" is defined in a descriptive way in the Slovak tax law. Rather then introducing the substantive definition, the law provides for a non-exhaustive list of instruments or transactions, the income from which is treated as interest for tax purposes.

The Income Tax Act refers in its sourcing rules (ZDP section 16 paragraph 1 letter E point 3) to interest and other income from provided loans, credits granted and deposits on bank accounts, proceeds from bonds, deposit certificates, treasury bills and similar securities and investment instruments.

The provision implementing the Directive and providing for exempting the qualified interest payments from taxation (ZDP section 13 paragraph 2 letter G) operates for the purposes of exemption of this income from taxation with the following definition: interest and other proceeds from loans and credits, share certificates, bonds, deposit certificates, treasury bills and other similar securities.

The two lists mentioned by the Income Tax Act are not mutually exclusive. The second list introduced by the implementing provision solely gives more examples of interest items, while both provisions contain the "similar" item provision, which extends the application on income items with similar nature or substance. In case of any doubts, for the purposes of the exemption, the second list mentioned would be applied.

The scope of the concept of interest under the Income tax Act appears to be sufficiently broad to cover the definition of interest under the Directive.

b. Exclusion of hybrid financial arrangements (Art. 4(1) b)-d))

The Slovak Republic did not exercise the option for exclusion of payments under financial arrangements listed in Art.4(1) b)-d) of the Directive from the beneficial treatment to be provided under the Directive.

c. Exclusion of interest reclassified as profit distribution or conflicting arm's length (Art. 4(1) a) and Art. 4(2))

The Slovak Republic did not exercise the option for exclusion of interest reclassified as profit distribution from the beneficial treatment to be provided under the Directive. Transfer-pricing rules potentially apply to interest payments not corresponding to the arm's length standard (see 1.2.1. *c. Transfer pricing*).

2.1.2. Concept of royalties

a. Definition

The Slovak Income Tax Act does not use the term "royalty", therefore there is no definition of royalty in general domestic tax law.

In absence of any domestic definition, the definition of royalties in the tax treaties could provide some guidance. The Slovak Income Tax Act lists the following types of income having source in the Slovak Republic and generally treated as royalties in the Slovak tax treaties:

- payments for the use of, or the right to use, any industrial property right, computer software, designs and models, plans, industrially technological and other economically exploitable knowledge (know-how) (ZDP section 16 paragraph 1 letter E point 1);
- payments for the use or the right to use of copyright or similar rights (ZDP section 16 paragraph 1 letter E point 2);
- rental payments for the use movable property located at the territory of the Slovak Republic (ZDP section 16 paragraph 1 letter E point 4).

The implementing provision covering the royalty payments (ZDP section 13 paragraph 2 letter l) operates only with reference to the items representing royalty income under the Directive. It lists payments for the use of, or the right to use, any industrial property right, computer software, designs and models, plans, industrially technological and other economically exploitable knowledge (know-how) (ZDP section 16 paragraph 1 letter E point 1).

Payments for copyright or similar rights are not listed in the implementing provision. These payments are subject to a 19% withholding tax. Please, note that under Art. 6 (1) of the Directive Slovakia has been authorised to apply the domestic rate of withholding tax with respect to royalty payments until 1 May 2006.

The list also does not include payments for the lease of industrial or commercial property (for tax treatment, see below).

b. Classification of revenue from leasing and software

Leasing payments are not referred to by the implementing provision (ZDP section 13 paragraph 2 letter l). These payments are be subject to collateral tax (see 1.2.1. *a. Outbound interest and royalty*). Please, note that under Art. 6 (1) of the Directive Slovakia has been authorised to apply the domestic rate of withholding tax with respect to royalty payments until 1 May 2006.

Payments for the use of computer software are listed as a type of payments benefiting from exemption under the Directive (ZDP section 13 para.2 letter l – referring to ZDP section 16 paragraph 1 letter E point 1). No further guidance has been issued with this respect.

c. Exclusion of royalties reclassified as profit distribution or conflicting arm's length (Art. 4(1) a) and Art. 4(2))

Excessive royalties that conflict the arm's length principle fall under the Slovak general transfer pricing rules (see 1.2.1. *c. Transfer pricing*). The provisions implementing the Directive do not exclude the excessive royalty from the applicability of the implementing provision.

2.2. COMPANIES

2.2.1. Types of companies benefiting from implementing provisions (Art. 3(a)(i))

a. Other types of entities

The implementing provisions do not limit application of benefits to any particular types of legal entities, both as to the payer and the recipient of income. The benefits under the implementing provisions are available to a wider range of legal entities than that in the Annex to the Directive.

Recipient of income

With respect to recipients of interest and royalty income, the exemption from withholding tax is only applicable if the recipient and the beneficial owner of the payment is a "legal entity, which is a taxpayer in another EU Member State".

The term "legal entity, which is taxpayer of an EU Member State" is defined as an entity that is subject to taxation in an EU Member State from income from the sources of that EU Member State as well as from sources outside of that EU Member State and, at the same time is not a taxpayer with unlimited tax liability in the territory of the Slovak Republic (ZDP section 2 letter T). Any legal entities resident for tax purposes in an EU Member State according to the tax laws of that EU Member State fall within the scope of the definition.

Payer of income

The implementing provision does not require that the payment is made by a qualified legal entity. The exemption will apply to any such payments having source on the territory of the Slovak Republic (ZDP section 13 paragraph 2 letters G and I). It means that also payments made by physical persons and transparent entities fall within the scope of the implementing provision.

b. Hybrid entities

Tax treatment of Slovak listed entities

The Slovak entities listed in the Directive (akciová spoločnosť, spoločnosť s ručením obmedzeným, verejná obchodná spoločnosť, komanditná spoločnosť, družstvo) are all the commercial entities that can be created under Slovak commercial law.

All of these entities are legal entities for civil and commercial law purposes. They are separate legal persons from their members, partners or shareholders. They can enter into contracts under their own legal name.

For tax purposes, Slovak joint stock companies (akciová společnost), limited liability companies (společnost s ručením omezeným) and cooperatives ("družstvo") have unlimited tax liability in the Slovak Republic. Different tax treatment applies to general partnerships (veřejná obchodní společnost) and limited partnerships (komanditní společnost).

General partnership is a legal entity, which generally is not subject to the Slovak corporate income tax. Its partners are jointly and severally liable for its liabilities under civil and commercial law. The partners are also subject to tax at their individual level, either as physical persons or companies. This entity may only act as a withholding agent of the final withholding tax applicable on certain payments (ZDP section 12 paragraph 4). This however does not make the entity subject to tax on its worldwide income. This entity is not considered a Slovak tax resident for tax treaty purposes.

Limited partnership, as such, is subject to Slovak corporate income tax only to the extent that their profits or losses are not attributable to the general partners (i.e. partners with unlimited liability, komplementári). The part attributable to the general partners is being taxed identically with the income derived by the partners of the general partnerships . Limited partnerships are generally treated as Slovak tax residents for tax treaty purposes.

Application of benefits to Slovak partnerships receiving the income

The application of the exemption to payments received by Slovak general and limited partnerships in other EU Member States may raise the issue of whether these entities comply with all the criteria of an associated company resident in an EU Member State set out in Art. 3 of the Directive. First, these two entities are included in the Directive, so at least one of the three conditions is met. Secondly, although these entities are not fully or partially subject to the Slovak company tax on their worldwide income, the income derived through these entities and attributed to their general partners will be subject to tax in the Slovak Republic irrespective of the fact, whether these entities actually are tax residents in the Slovak Republic or not, because any income derived through these entities by their general partners would be subject to tax in the Slovak Republic under the "deemed permanent establishment" provision (ZDP section 16 paragraph 3). Under Slovak rules, income from Slovak partnerships attributed to non-resident general partners is deemed to be the income derived through a Slovak permanent establishment. Thus, the worldwide income derived through these entities will be subject to tax in the Slovak Republic, either to corporate or individual income tax, as the case may be.

The inclusion of these entities into the Annex to Directive may in practice result in situations, when another EU Member State will be providing benefits under the Directive to individuals acting as general partners of these entities.

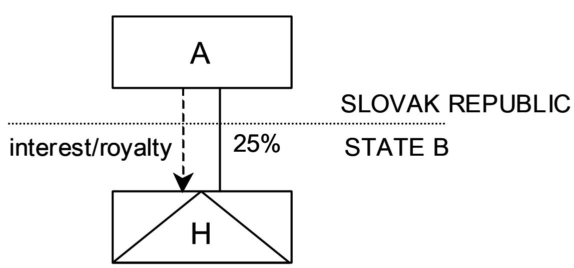
Application of benefits to hybrid entities by the Slovak Republic

The issue of tax treatment of payments in situations involving hybrid entities is considered based on three hypothetical situations described below:

- Case 1: a Slovak entity pays interest and royalties to a hybrid entity H located in Member State B;
- Case 2: a Slovak hybrid entity H pays interest and royalties to an associated company in Member State A;
- Case 3: a Slovak entity pays interest and royalties to an associated company through a hybrid entity H, the latter two located in Member State A.

Case 1: Payment to a hybrid entity

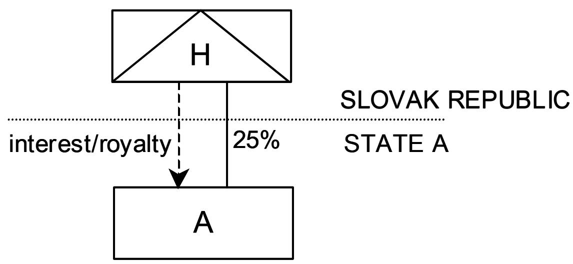
A Slovak entity A pays interest and royalties to a hybrid entity H situated in Member State B. The Slovak Republic treats hybrid entity H as a transparent entity.



In this case the benefits under the Directive would be granted, provided that the foreign hybrid entity meets the above mentioned criteria of a "legal entity, which is taxpayer of an EU Member State". If the foreign hybrid entity fails to present the necessary proof that the conditions are met (tax residence requirement, subject-to-tax requirement, etc.), the exemption would not be granted. There are however no attestation requirements (see 3. PROCEDURE below).

Case 2: Payment from a hybrid entity

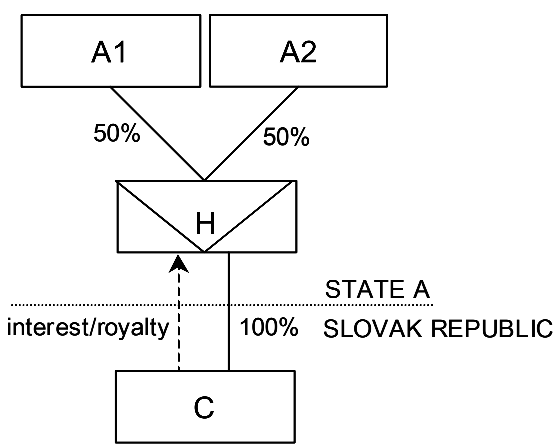
A hybrid entity H in the Slovak Republic pays interest or royalties to an associated company A in Member State A.



In this case the benefits will apply because the relief applies irrespective of the form of the payer of income (ZDP section 13 paragraph 2 letter l). Slovak general partnerships and limited partnerships, as well as Slovak permanent establishments of foreign transparent entities will fall within the scope of the implementing provisions.

Case 3: Payment through a hybrid entity

Companies A1 and A2 are the members of the hybrid entity H, all located in Member State A. The hybrid entity H holds all the shares in company C, located in the Slovak Republic. The Slovak Republic treats hybrid entity H as a transparent entity. Company A1 grants a loan to the hybrid entity H and the hybrid entity H grants a loan to the company C. Interest flows from the company C to a member A1 through the hybrid entity H.



The tax treatment in this case is identical to that set out for Case 1.

2.2.2. Residence requirement (Art. 3(a)(ii))

a. Implementation of the requirement

To qualify for the benefits under the Directive, the recipient of the income must be a "legal entity, which is taxpayer of an EU Member State" (ZDP section 13 paragraph 2 letters G and I).

The definition (for full definition see 2.2.1. *a.*) of the term "legal entity, which is taxpayer of an EU Member State" is introduced in the provision (ZDP section 2 letter T). This term includes entities that are not tax resident under Slovak income tax law and are subject to tax on its worldwide income in an EU Member State. The definition does not contain any further reference to the residency for tax purposes as per the terms of a tax treaty concluded with a third state. It is not required to investigate whether, under a tax treaty with a third state outside of the EU, an entity is considered to be a resident of that third state outside of the EU.

There is no requirement to obtain a specific proof that the recipient qualifies as a tax resident of an EU Member State to apply the relief. In practice the payer would probably request a certificate of residency to prevent liability to collect withholding tax.

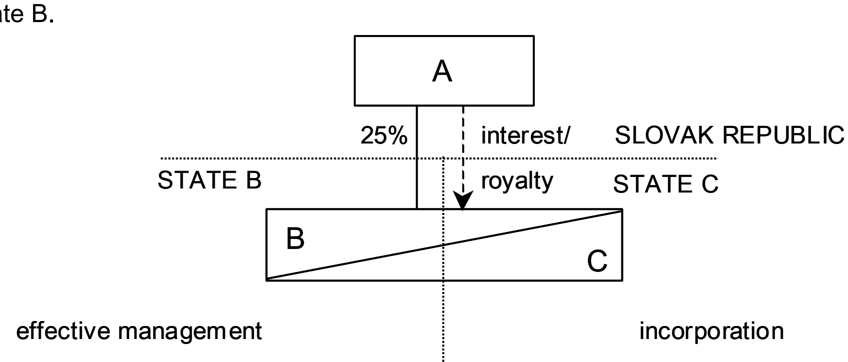
b. Application of the requirement in dual residence cases

There is no specific guidance with respect to application of exemption from withholding tax when interest or royalties are paid to or from dual resident companies between Member States. The conclusions on the tax treatment of such payments are drawn on the basis of general implementing provisions of the Income Tax Act. The issue of tax treatment of payments in situations involving dual residency is considered based on three situations described below:

- Case 1: a Slovak associated company A makes an interest or royalty payment to a dual resident company BC incorporated in Member State C but with its effective management in State B;
- Case 2: a dual resident company BC incorporated in Member State C but with its effective management in the Slovak Republic makes an interest or royalty payment to an associated company A resident in Member State A;
- Case 3: a dual resident company BC incorporated in Slovak but with its effective management in State C makes an interest or royalty payment to an associated company A located in Member State A.

Case 1: Payment to a dual resident

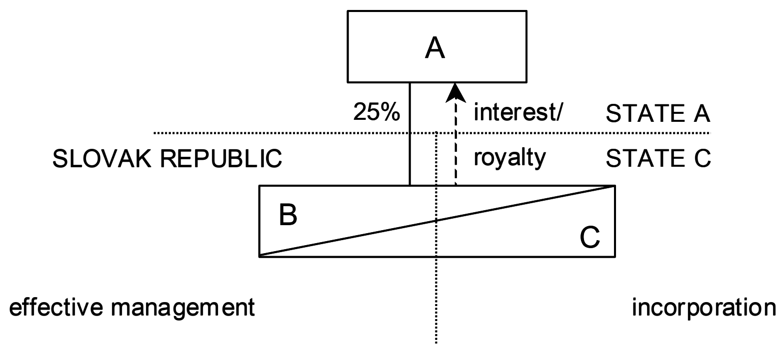
A Slovak associated company A makes an interest or royalty payment to a dual resident company BC incorporated in Member State C but with its effective management in Member State B.



In this case the benefits of the Directive would be granted, because the company meets the condition of being resident in another Member State and subject to worldwide taxation at least in one of the two states.

Case 2: Payment by a dual resident with the place of management in the Slovak Republic

A dual resident company BC incorporated in Member State C but with its effective management in the Slovak Republic makes an interest or royalty payment to an associated company A resident in Member State A.

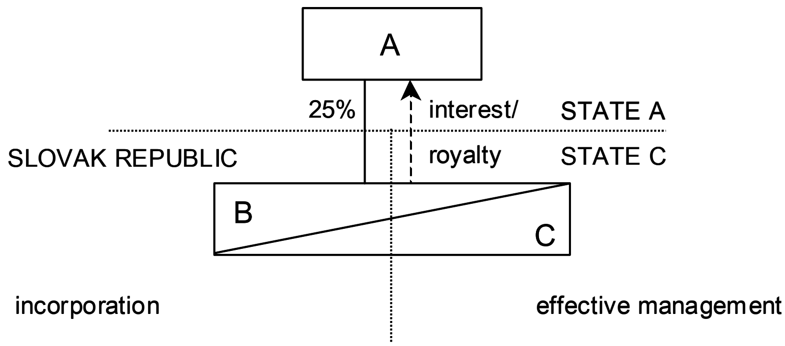


In this case, the situation would be resolved by the application of the tie-breaker rules contained in a tax treaty, assigning the residence of the company either to the Slovak Republic or to the other Member State. It must be noted, that it is not always the place of effective management criteria, e.g. in relation to the Baltic States (Estonia, Latvia and Lithuania) the place of effective management criterion is absent and replaced by the mutual agreement procedure.

In any case, since the Slovak tax law links the benefits under the Directive to the income having source in the Slovak Republic the dual resident company BC would have to be subject to worldwide taxation in Slovakia or, if not, have its permanent establishment in Slovakia to qualify for the benefits of the Directive. Thus in situations, when as a result of applying the tax treaty tie-breaker rules, the company would not be considered a resident of the Slovak Republic, but of the other Member State, the Slovak Republic could tax such income only in situation, when the income is borne by the Slovak permanent establishment of the non-resident company (including a permanent establishment of a company resident in a third state). A company would normally have a permanent establishment when it has the place of effective management in the Slovak Republic. If however for any reasons such a company does not have a permanent establishment in Slovakia, and is considered to be tax resident in State C under the tax treaty, the income would not have source in Slovakia. It would not trigger the application of the sourcing rules and would not be subject to withholding tax.

Case 3: Payment by a dual resident with the place of incorporation in the Slovak Republic

A dual resident company BC incorporated in the Slovak Republic but with its effective management in State C makes an interest or royalty payment to an associated company A located in Member State A.



In this case the Slovak Republic would grant the benefits under the Directive for the reasons similar to those stated for Case 2 above.

2.2.3. Subject-to-tax requirement (Art. 3(a)(iii))

The definition of the term "legal entity, which is taxpayer of an EU Member State" includes entities that are not subject to worldwide taxation under Slovak income tax law and are subject to worldwide taxation in the other Member State (for full definition see 2.2.1. *a. Other types of entities*). No other requirement is stipulated. There is also no reference to particular taxes listed in Art. 3 a. of the Directive.

It appears that the subject-to-worldwide taxation requirement relates to the company itself and not to the particular income received and covered by the Directive.

There have been no instances reported when the Slovak Republic refused to accept an assurance by the residence state of the "beneficial owner" that the latter is subject to tax in its Member State.

No specific subject-to-tax criterion applies in the case of hybrid entities as recipients of the income in question. To obtain the benefits under the Directive, hybrid entities must comply with the same requirements as the other legal entities, i.e. to be subject to worldwide taxation in another EU Member State.

2.2.4. Associated company (Art. 3(b))

The implementation provisions make the granting of the benefits under the Directive subject to the condition of payment taking place between associated persons. The person making the payment and the recipient of the payment must be parties directly related by capital. The provisions implementing the Directive (ZDP section 13 paragraph 2 letters G and I) require the holding thresholds as follows:

- the taxpayer (here also physical person) making the payment shall hold at least 25% direct share in the registered capital of the beneficial owner of the payment, or
- the beneficial owner of the payment holds at least 25% direct share in the registered capital of the taxpayer making the payment, or
- other legal entity with its seat in EU Member State holds at least 25% direct share in the registered capital of the company making the payment and at the same time at least 25% direct share in the registered capital of the beneficial owner of the payment.

It shall be noted that in the last case, the law refers to the seat of the legal entity. The term “seat” is normally understood as the legal address. It may lead to the conclusion that the place of management, which may be decisive for determining the residency for tax purposes, could be disregarded and the holding company could be a tax resident outside the EU. However, there has no official guidance issued with respect to interpretation of the term.

The holding of capital requirement provides only for holding of share capital.

The Slovak Republic thus does not apply a lower ownership threshold than the one in the Directive and it did not exercise the option of replacing the requirement of holding in capital with that of the voting rights provided for in Art. 1 (10) of the Directive. There is no general extension of benefits to situations of indirect holdings.

2.2.5. Beneficial ownership (Art. 1(4))

The implementation provisions make the granting of the benefits under the Directive subject to the condition that the recipient is the beneficial owner (final recipient – literal translation from Slovak) of the income (ZDP section 13 paragraph 2 letter G and I). The definition itself has not been incorporated.

The implementation provisions newly include the term "beneficial owner" for the first time in Slovak income tax law. Until recently, this term was only used in the double taxation treaties concluded by the Slovak Republic. Since the term literally translated from Slovak means a “final recipient" of the income, it can be interpreted so that conduit or other types of arrangements would be not entitled to the benefits from the Directive. There are however no arrangements in place to enforce the principle.

The condition that the recipient of the income must be subject to unlimited taxation in another EU Member State needs to be met in conjunction with the beneficial ownership requirement, which is the only link between the "subject-to-tax" and beneficial ownership requirements.

2.3. PERMANENT ESTABLISHMENTS

2.3.1. Definition (Art. 3(c))

There were no specific provisions introduced in the context of implementation of the Directive in respect to definition of permanent establishment. Therefore the general concept of permanent establishment under the general tax law applies, with the limitations introduced by a particular tax treaty.

A permanent establishment is defined as permanent place or equipment (installation) for performance of activities, through which the taxpayers with limited tax liability exercise fully or partially their activities on the territory of the Slovak Republic (ZDP Section 16, paragraph 2). This includes, in particular, the place from which the activities are organized (managed), branch, office, workshop, workplace, place of sales, technical equipment or place for research or mining of natural resources. The place or equipment is considered to be permanent, if it is being used all the time or repeatedly. In the case of one-off activity, the place or equipment is considered to be permanent when the activities are exercised for the period exceeding 6 months (either consecutively or not) during a period of any 12 consecutive months. A construction site and site of provision of construction services (such as preparation of architectural plans) is regarded as a permanent establishment only if their duration exceeds an uninterrupted period of 6 months.

A person, who acts in the name of a non-resident taxpayer and permanently or repeatedly negotiates or concludes contracts in its name on the basis of his authorisation also leads to a permanent establishment. The person is considered to act in the name of a taxpayer, when he acts on the basis of its instructions while the taxpayer controls the result of activities and bears the entrepreneurial risks.

In addition, the income derived by a non-resident general partner of a partnership with respect to the participation, or from credits and loans granted to a Slovak partnership, is treated as income from a permanent establishment (ZDP Section 16 paragraph 3). The permanent establishment of a partner in partnership arises also in situations when the non-resident partner does not personally visit the country. Interest on credits or loans granted to the partnership by the partner (a company of a Member State) will be also treated as income from a Slovak permanent establishment.

The domestic law does not contain an exception for auxiliary activities; therefore a permanent establishment could arise also in situations, when such auxiliary activities are performed on the territory of the Slovak Republic, unless restricted by the applicable tax treaty. Since Slovak Republic concluded tax treaties with all the Members States following the OECD MC, the exception for auxiliary activities would effectively apply in relation to enterprises resident in the other Member States.

2.3.2. Application of source rules (Art. 1(2))

In the case of the Slovak Republic, the domestic definition of permanent establishment is generally broader or more detailed than the definition set out in the Art. 3 (c) of the Directive.

The Slovak Republic would levy a withholding tax on the income covered by the Directive only if it was paid by the Slovak permanent establishment of non-resident enterprises as defined by the Slovak tax law (with applicable tax treaty limitations) or by the persons subject to worldwide tax liability in the Slovak Republic. The Slovak Republic would thus not levy the withholding tax on the income covered by the Directive unless it was borne by the Slovak tax resident or by the permanent establishment as defined by the Slovak tax law.

In addition, under the tax treaties concluded with all the Member States, the sourcing rule related to the payments of interest resembling Art. 11 (5) of the OECD MC would prevent the Slovak Republic to levy a withholding tax on such interest, unless such interest would be deemed to arise on the territory of the Slovak Republic.

2.3.3. 'Tax-deductible expense' requirement (Art. 1(3))

The ‘tax-deductible expense’ requirement set forth in Art. 1 (3) of the Directive has not been explicitly implemented into the Slovak tax law. Currently, the Slovak tax law does not require interest or royalty payment to be deductible for tax purposes in order to qualify for an exemption.

Due to the absence of this requirement, the benefits of the Directive would be therefore generally granted even if the income covered by the Directive is not allowed as a tax-deductible expense.

2.3.4. Beneficial ownership (Art. 1(5))

The Slovak tax law does not particularly address the issue of the beneficial ownership in relation to permanent establishments.

The implementing provisions only make the benefits under the Directive conditional by the fact that the recipient of the income is also a beneficial owner of that income and that it is a "legal entity, which is taxpayer of an EU Member State". The implementing provisions do not make a distinction between the head office or the permanent establishment being the beneficial owner of income.

It follows that the general rules related to the beneficial ownership of the income by the "company that is resident in another Member State" apply to permanent establishments (see 2.2.5. Beneficial ownership). Since the Slovak Republic applies the beneficial ownership test for companies under Art. 1 (4) of the Directive with respect to permanent establishments, there is no specific requirement for the income to be 'effectively connected' or 'subject-to-tax'. It thus might be possible that interest or royalties, while beneficially owned by "company that is resident in another Member State" which is "subject to tax listed in the Directive", are not be subject to tax anywhere. This would be the case when, e.g., this income is not taxed in the Member State of the receiving permanent establishment and a head office state operates an exemption system with respect to the income of permanent establishments located abroad.

2.3.5. Permanent establishment in a third country (Art. 1(8))

The Slovak implementing provisions of the Directive do not provide for the limitation of the benefits under the Directive in a situation where the income covered by the Directive is attributable to a permanent establishment located on the territory of a third country. Interest or royalties paid to a third-country permanent establishment of an associated company, which is a taxpayer in an EU Member State thus seems to fall within the scope of the implementing provisions and will benefit from the relief.

3. PROCEDURE

The Slovak Republic requires a 24-month holding period. The application of benefits is not conditional upon attestation or decision of the tax authorities. The exemption is applied at source. No specific refund procedures has been introduced in Slovak income tax law in connection with the implementation of the Directive.

3.1. MINIMUM HOLDING PERIOD (ART. 1(10))

3.1.1. General

The benefits from the Directive are granted only if the entity making the payment and the recipient of the payment are parties directly related by capital and this relation lasts for an uninterrupted period of at least 24 consecutive months at the time the payment is made.

3.1.2. Relief before the holding period requirement is satisfied

The benefits cannot be granted prior to expiry of this period.

If the condition is not fulfilled, both the recipient and the payer of the income will be subject to the tax liability. In the case of the recipient (the taxpayer), it will be considered as a failure to meet his tax liability. As for the payer of income (withholding agent), the amount of the tax, which was not withheld, can be claimed as this companies liability (ZDP section 43 paragraph 12).

3.1.3. Appeals

There is no specific provision governing the appeal of a decision not to regard the requirement of holding as being fulfilled. There is however the possibility to appeal any decision of the tax authority under the general tax procedure provisions.

3.2. ATTESTATION (ART. 1(11) AND 1(13))

To obtain the benefits under the Directive the recipient of the income does not need to submit an attestation.

3.3. DECISION ON APPLICATION OF THE RELIEF (ART. 1(12))

To obtain the benefits under the Directive the recipient of the income does not need to obtain for a ruling from the tax administration.

3.4. APPLICATION FOR REFUND (ART. 1(15) AND 1(16))

There was no specific refund procedure introduced in Slovak income tax law in connection with the implementation of the Directive.

3.4.1. General

Although there was no specific refund procedure introduced in Slovak income tax law in connection with the implementation of the Directive, in the case, where all the conditions for the exemption were met and the payer nevertheless withheld the tax, the tax so withheld could be considered as the excessive tax paid (ZSDP section 63). In such a case, the taxpayer may apply for repayment of the excessive tax paid under the general procedure while proving that all the conditions for the exemption were fulfilled.

The tax authorities must refund any overpaid amounts in one month or issue a decision refusing to make a refund.

If the tax authorities are in default, the default interest is three times the primary rate of the Slovak National Bank.

These general rules equally apply to residents or non-residents.

3.4.2. Appeals

In case the tax administration refused to repay the excessive tax paid, there is a 15-day appeal period, when the taxpayer has a right to appeal this decision with the tax authority.

4. FRAUD AND ABUSE (Art. 5)

4.1. MEASURES UNDER ART. 5(1) OF THE DIRECTIVE

4.1.1. Domestic

The Slovak tax legislation does not include any specific anti-abuse provisions relating to the Directive. The general substance-over-form rule allowing tax authorities to take into account the substance of a particular transaction and to disregard the formal structuring of the transaction could be used to prevent fraud or abuse (ZSDP section 2 paragraph 7). Further, the Tax Administration Act contains a general anti-avoidance provision allowing the tax authorities to use their own assessment when determining the tax base of the taxpayer, who performed operations that by their substance or purpose were aimed against the specific law or were aimed to circumvent a specific law, and which resulted in reduction in the tax base (ZSDP section 23d).

The implementation of the Directive introduced the term "beneficial ownership", without defining this term further.

4.1.2. Agreement-based

Slovak tax treaties do not include any specific anti-treaty-shopping provision. Most of Slovak treaties include the term "beneficial ownership".

4.2. MEASURES UNDER ART. 5(2) OF THE DIRECTIVE

The implementation provisions newly included the term "beneficial ownership" into the Slovak income tax law. However, no specific anti-Directive-shopping rule was adopted. There is also lack of any case law giving guidance on how to properly interpret the "beneficial ownership" requirement.

4.3. COMPARISON WITH SIMILAR MEASURES UNDER PARENT-SUBSIDIARY AND MERGER DIRECTIVES

There were no specific anti-abuse provisions introduced in relation to the Parent-Subsidiary and Merger Directives. See, however, also under 4.1.1.

5. SUMMARY

The Slovak Republic generally implemented the Directive in relation to interest payments.

In relation to royalty payments, Slovakia has been authorized to apply a domestic withholding tax until 1 May 2006. Slovakia adopted the rules exempting royalty payments, effective as of 1 May 2006. The implementation appears not to be complete with respect to the concept of royalties (see below). Please note, however, that until the expiry of the transitional period, royalty payments under the Directive are subject to the domestic withholding tax.

Scope

The concept of interest under Slovak implementing provisions appears to be sufficiently broad to cover the concept under Art. 2 of the Directive. There is no definition of royalty payments in Slovak income tax law. The implementing provision does not include leasing payments, which are subject to a collateral withholding tax.

The Slovak Republic has not restricted the benefits of the Directive to particular types of entities listed in the Annex to the Directive. The benefits have been extended to payments made by any tax resident of the Slovak Republic (including individuals and permanent establishments of companies resident in third countries) to legal entities of any type resident in an EU Member State.

As to tax residency of the recipients of income, the Slovak law requires an entity to be subject to tax on worldwide income in an EU Member State. It does not incorporate the requirement not to be tax resident in a third country under a tax treaty between a Member State and the third country. The requirement to be subject to taxes listed in Art. 3 (a) (iii) of the Directive has not been transposed.

The association criteria are similar to those listed in Art. 3 of the Directive. However, it appears that a situation where a company with its seat in Slovakia but resident in a third state holds shares in two companies resident within EU may also qualify. The Slovak Republic has not replaced the holding of the capital requirement with that of the voting rights.

Procedure

A 24-months holding period at the time of payment is required. The benefits are not available before the holding period requirement is met.

The Slovak Republic adopted the system of automatic application of the benefits under the Directive at source. General refund rules may be invoked to refund any excessive taxes withheld from interest or royalty payments.

Fraud and abuse

There have been no specific anti-abuse provisions introduced in relation to the Directive, except for the requirement of the “beneficial ownership”. The tax authorities may be able to invoke the general anti-abuse provision (substance over form).

PART II. THE AGREEMENT

For a period of time it was not exactly clear what measures should be appropriate with respect to Agreement between the European Community and the Swiss Confederation providing for measures equivalent to those laid down in Council Directive 2003/48/EC on taxation of savings income in the form of interest payments (the "Agreement").

Eventually, the Ministry of Finance of the Slovak Republic issued an information note on the 8 September 2005 on the taxation of income from savings in the form of payments of interest on the basis of Agreements between the Slovak Republic and the dependent territories of the EU Member States and the Agreements between the EU and the third states.

The note contains the reference to Article 15 of the Agreement and informs that it would apply in the Slovak Republic as of 1 July 2005.

The relevance of the Agreement is to a certain extent limited in relation to the Directive, because the 2-year transitional period on royalties, which will apply in relation to Switzerland similarly as in relation to the other EU Member States. In relation to interest payments, the current tax treaty between Switzerland and the Slovak Republic provides for limited taxing rights of the state of source (10% withholding tax), therefore in relation to interest payments the Agreement is crucial.

ANNEX

Table of the maximum withholding tax rates on interest and royalty payments under the tax treaties between the Slovak Republic and the EU Member States

EU Member State	Interest	Royalties
Austria	0	0/5 <2>
Belgium	10 <1>	5
Cyprus	10	0/5 <2>
Czech Republic	0	10
Denmark	0	0/5 <2>
Estonia <6>	10	10
Finland	0	0/1/5/10 <3>
France	0	0/5 <2>
Germany	0	5
Greece	10	0/10 <2>
Hungary	0	10
Ireland	0	0/10 <2>
Italy	0	0/5 <2>
Latvia	10	10
Lithuania	10	10
Luxembourg	0	0/10 <2>
Malta	0	5
Netherlands	0	5
Poland	10	5
Portugal	10	10
Slovenia	10	10
Spain	0	0/5 <4>
Sweden	0	0/5 <5>
United Kingdom	0	0/10 <2>

<1> The lower rate applies, inter alia, to interest on bank loans and deposits.
<2> The higher rate applies to industrial royalties.
<3> Copyright royalties are exempt; the 1% rate applies to royalties paid for finance leases of equipment; the 5% rate applies to royalties paid for the use of computer

software and operational leases of equipment; the 10% rate applies to industrial royalties in general.

<4> The lower rate applies to copyright royalties, excluding film royalties.

<5> The lower rate applies to copyright royalties, including film royalties.

<6> The treaty is concluded, but not yet in force.

UPDATE FOR THE SLOVAK REPUBLIC

The amendments of the Slovak Income Tax Act amending, *inter alia*, the scope of payments qualifying for the treatment of royalties for the purposes of the Directive were published in the Collection of Laws on 3 December 2005 under number 534/2005 Coll. The amendment to the list in section 13 paragraph 2 letter l of the Income Tax Act will become effective as of 1 May 2006.

The amendment extends the scope of qualified payments, which may benefit from the exemption granted under the Directive, to include remunerations for the use of, or for the right to use, industrial, business, or scientific equipment and remunerations for the use of, or for the right to use copyright or similar rights. The current definition of royalties under the Income Tax Act does not include these types of royalty payments (see 2.1.2. Concept of royalties of the country report). This amendment aims to bring the Slovak tax law in line with concept of royalties set out in the Directive by the expiry of the transitional period granted to the Slovak Republic under Art. 6 of the Directive with respect to royalty payments.