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Recent Developments in International Taxation

Serbia

Tomislav Popovic

BDK Advokati AOD

[Tomislav.popovic@bdkadvokati.com](mailto:Tomislav.popovic@bdkadvokati.com)

## **Recent highlights**

Since May 2018 and until the date of this report, the most significant tax development with an international dimension which has occurred in Serbia involves ratification and entry into force of the OECD Multilateral Convention to Implement Measures to Prevent Base Erosion and Profit Shifting (“**BEPS**”). Another important development is a corporate income tax reform, which resulted in introduction of the IP box regime and other corporate income tax incentives for R&D activities and innovative startups, as well as in certain incentives for businesses in general. Furthermore, the Ministry of Finance has recently made an official announcement that Serbia intends to join OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters by the end of 2019. Finally, Serbia has ratified additional DTTs.

### **OECD Multilateral Convention to Implement Measures to Prevent BEPS (“MLI”)**

The MLI was ratified in the Serbian Parliament on 19 April 2018. Serbia deposited its ratification instrument on 5 June 2018, and the MLI became effective and binding on Serbia on 1 October 2018.

The MLI modifies the existing double taxation treaties (“**DTTs**”) of Serbia without the need to negotiate, sign and ratify the amendments of such DTTs. Serbia notified the OECD Secretariat that it wants 64 of its DTTs (almost all) covered by the MLI. The Ministry of Finance published on its webpage seven of Serbia’s DTTs in the consolidated version modified pursuant to the MLI, namely DTTs with Austria, France, Lithuania, Poland, Slovak Republic, Slovenia and the UK (modified versions pursuant to the MLI of these DTTs are effective from 1 January 2019).

### **Amendments to Corporate Income Tax**

On 9 December 2018, the amendments to the Corporate Income Tax Act (“**CITA**”) came into force. Most of the amended provisions will be applicable starting from the fiscal year 2019.

#### ***Tax depreciation rules reform***

Significant changes were made to the rules on tax depreciation of assets. These new rules will apply with respect to assets acquired from 1 January 2019. Before the changes, moveable assets were classified in four depreciation groups where the basis for depreciation was the group balance and the method applied was declining balance method. Under the new rules, all assets, immovables and movables, are to be depreciated by using the straight-line method, the basis being the acquisition value of each individual asset. If depreciation under the accounting rules (accounting depreciation) results in the lower depreciation expense than the depreciation calculated under tax rules, the accounting depreciation will be recognised for tax purposes.

Accounting depreciation of intangibles will be fully recognised for tax purposes and therefore there is no need to calculate tax depreciation for intangible assets.

#### ***Advertising expenses fully recognised***

Advertising expenses used to be recognised as deductible expenses only up to certain small percentage of the total annual revenue (10% and previously 5% of the total annual revenue). This limitation applied to all corporate taxpayers regardless of their business or industry. The 2018 amendments finally deleted this limitation allowing for the full deductibility of advertising and marketing expenses starting from the fiscal year 2019.

#### ***IP Box regime and incentives for financing innovation startups introduced***

Amendments introduce an IP box or patent box regime and incentives for funding innovation startups. There are three types of incentives:

- Double deduction of qualified expenses directly connected to research and development (“**R&D**”) activity carried out in the country;
- Partial exemption of income from licensing of copyright-protected works of arts and science (including software, which is protected by copyright), “neighbouring rights”, rights from inventions and patent applications deposited or filed with the Serbian IP office;
- Tax credit for injecting cash in the equity of the innovative start-ups having principal place of business in Serbia.

#### Double recognition of qualified R&D expenses

Expenses that are directly connected to scientific or technical R&D activity carried out in Serbia can be deducted in a double amount for tax purposes. R&D activity is any research and development carried out with the aim of acquiring new scientific or technical knowledge or implementing such knowledge by creating new or improved products, materials, services, processes prior to their commercial exploitation. Activities related to exploration and extraction of oil, gas and minerals are excluded.

The Minister of Finance is authorised to adopt an implementing regulation setting out the details of this preferential regime. He has not done so by the date of this report.

#### Partial (80%) exemption of income from copyright, inventions and patent applications

Taxpayers who hold title to copyright-protected creative artistic, literary, scientific and professional works, and/or so-called “neighbouring rights” (rights of performers, publishers, phonogram producers, broadcasters etc.), including software (which is also protected by copyright) deposited with the Serbian IP Office (“**Qualified IP Rights**”) can opt for a partial exemption of qualified income generated, starting from 1 January 2019, from licensing of the Qualified IP Rights (“**Qualified Income**”). Rights related to technical inventions and patent applications filed with the Serbian IP Office are also regarded as the Qualified IP Rights, and income generated through licensing of such rights is also regarded as the Qualified Income.

Qualified Income is calculated as follows:

- related tax-deductible historical and current expenses for R&D that have led to creation of the Qualified IP Rights (“**Qualified Expenses**”) are deducted from the total income from Qualified IP Rights;
- Ratio between the total expenses in relation to the Qualified IP Rights and Qualified Expenses is established;
- The same ratio is used to determine the Qualified Income, which is a pro-rata portion of the total income from the Qualified IP Rights.

Once when the Qualified Income is determined, 80% of it represent an amount that is exempt from the tax base (only 20% of it is included in the tax base). Also, in case of a sale of the entire Qualified IP Right only 20% of the capital gain will be taxable (80% of the capital gain will be exempt).

The amendments introduce an obligation on taxpayers to separately present income from the Qualified IP Rights in their tax returns, as well as to maintain documentation proving the Qualified IP Rights, Qualified Expenses and Qualified Income. The Minister of Finance is given authority to adopt implementing regulations setting out in more details the manner of calculation and exemption of the Qualified Income and the documentation to be kept by the taxpayers to prove it, relying on the

relevant OECD documents regarding IP-related tax incentives. By the date of this report, such implementing regulations have not been adopted.

#### *Tax credit for cash equity injections in the innovative start-ups*

Taxpayers which invest cash in the equity of the newly established companies carrying out innovative business are entitled to a tax credit (reduction of corporate income tax) in an amount corresponding to 30% of the investment made, but not more than RSD 100 million per investment by a single taxpayer into a single “innovative company” and not more than RSD 50 million in total per single taxpayer in single fiscal year.

“Innovation companies” are companies which were established three years or less prior to the date of investment, and which predominantly carry out innovation business as defined in the Innovation Business Act. Innovation is creating new or significantly changing existing products, technologies, processes, or services for commercial use. An innovation company must also fulfil the following conditions:

- (i) total revenue in the last financial year does not exceed RSD 500 million;
- (ii) it has not distributed dividends since its incorporation and will not distribute dividends within the period of three years from the date of investment;
- (iii) Serbia is the center of its business activities;
- (iv) it has not been established through a corporate reorganisation in accordance with the Companies Act; and
- (v) in each fiscal year, starting from the year following the year of incorporation and until the year in which the investment is made, it satisfies at least one of the following three conditions:
  - its R&D expenses are accounting for at least 15% of the total costs, or
  - highly qualified people make up more than 80% of all employees, or
  - it is the owner or user of a copyright deposited with or patent registered with the Serbian IP Office, which copyright or patent is directly connected with the innovation business the company carries out.

The tax credit is available to taxpayers which have not held prior to injecting cash contributions to the equity of the “innovation companies” (alone or jointly with related entities) more than 25% of shares or voting rights in such companies. To address possible abuses, the amendments provide that the tax credit is available only under the condition that the investor has not reduced the capital of the “innovation company” during the period of three years from the date of contribution.

#### **New DTTs**

On 1 January 2019, new DTTs with Indonesia and San Marino came into effect. San Marino used to be blacklisted as a tax haven jurisdiction under the ordinance adopted by the Minister of Finance, however effective from 1 January 2019 it was removed from the blacklist.

On 22 November 2018, the new DTT was signed with Israel. Serbia ratified it on 18 February 2019. The entry into force is expected on 1 January 2020.

#### **OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters**

On 27 March 2019, the Ministry of Finance announced that Serbia is planning to sign and ratify the OECD Multilateral Convention on Mutual Administrative Assistance in Tax Matters. It was also stated in a press release that the implementation of the automated information exchange is expected in the

future, as soon as the necessary technical conditions are fulfilled (e.g. IT infrastructure ensuring protection of exchanged data, internal rules and procedures for handling and protection of information). However, it was emphasised in the press release that the implementation of automated data exchange is not a precondition to the signing of the convention and that Serbia already implements information exchange upon request and spontaneous exchange on the basis of the signed and ratified DTTs.