

# The International Comparative Legal Guide to: Corporate Tax 2010

A practical insight to cross-border Corporate Tax work



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# Bulgaria



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### 1 General: Treaties

#### 1.1 How many income tax treaties are currently in force in Bulgaria?

Bulgaria has 66 double tax treaties in force.

#### 1.2 Do they generally follow the OECD or another model?

The double tax treaties follow the OECD model except for the treaty with the USA which follows the US model.

#### 1.3 Do treaties have to be incorporated into domestic law before they take effect?

The treaties have to be ratified and their texts published in the official press in order for them to become a part of the Bulgarian legislation.

#### 1.4 Do they generally incorporate anti-treaty shopping rules (or "limitation of benefits" articles)?

The double tax treaties to which Bulgaria is a party, with the exception of the treaty with the USA, do not usually contain anti-treaty shopping rules.

Bulgarian revenue authorities, however, may apply domestic anti-avoidance rules.

#### 1.5 Are treaties overridden by any rules of domestic law (whether existing when the treaty takes effect or introduced subsequently)?

Treaties override any rules of domestic law.

### 2 Transaction Taxes

#### 2.1 Are there any documentary taxes in Bulgaria?

No, there are not.

#### 2.2 Do you have Value Added Tax (or a similar tax)? If so, at what rate or rates?

Bulgaria has introduced value added taxation. The general VAT rate is 20%. A reduced rate of 7% is applicable to accommodation by a

hotel-keeper provided as part of an organised journey.

#### 2.3 Is VAT (or any similar tax) charged on all transactions or are there any relevant exclusions?

Bulgarian VAT regulations follow EU VAT directives.

Transactions with goods or services having a place of supply in Bulgaria are deemed VAT-able.

Exports from the EU are zero-rated.

The concepts "intercommunity supplies/acquisitions of goods" are also introduced.

There are also VAT-exempt supplies that can generally be grouped into the following categories: (i) hospital and medical care; (ii) the supply linked to welfare and social security work; (iii) supplies linked to education, sports or physical education; (iv) supplies linked to cultural activities; (v) supplies by religious or philosophical institutions linked to religious activities; (vi) supplies having non-commercial nature made by organisations with aims of political, religious or civic nature provided that this exemption is not likely to cause distortion of competition; (vii) certain supplies with land and buildings; (viii) certain financial services supplies; (ix) insurance supplies; (x) gambling; (xi) public postal services; and (xii) supplies with goods and/or services for which a VAT credit has not been available.

#### 2.4 Is it always fully recoverable by all businesses? If not, what are the relevant restrictions?

VAT shall be fully recoverable if the business performs VAT-able supplies only.

Generally, unless otherwise provided under the Bulgarian VAT Act, for the purposes of VAT recoverability, VAT-able shall be deemed: (i) supplies with a place in Bulgaria; (ii) zero-rated supplies; and (iii) supplies with a place of supply outside Bulgaria, which would have been VAT-able, if they had been performed on the territory of Bulgaria, etc.

Restrictions on VAT recovery are generally applicable when the taxable person uses the purchased goods or services for making exempt supplies, supplies without consideration, supplies not related to person's business, supplies for representative or entertainment purposes as well as on purchase of automobiles.

#### 2.5 Are there any other transaction taxes?

##### Real Estate Transfer Taxes

The real estate transactions in Bulgaria are subject to the following

taxes and stamp duties: (i) real estate transfer tax - from 1.3% to 2.6% (the percentage varies in the different municipalities); (ii) real estate registration stamp duty - 0.1%; and (iii) notary fees - based on progressive table (not exceeding EUR 3,000). The taxes and stamp duties are levied on the selling price or on the tax evaluation, whichever is higher. The taxes and stamp duties are paid prior to/at the time of the acquisition.

#### Motor Vehicle Transfer Tax

The transfer of a motor vehicle is subject to 1.3% to 2.6% transfer tax (the percentage varies in the different municipalities) and notary fees.

### 2.6 Are there any other indirect taxes of which we should be aware?

Custom duties are generally payable on goods imported from outside the EU.

The following goods are subject to excise duty: (i) alcohol and alcohol beverages; (ii) tobacco products; and (iii) energy products and electricity. As of January 1st 2010 excise duties on motor vehicles will be abolished.

There are also certain environmental taxes.

## 3 Cross-border Payments

### 3.1 Is any withholding tax imposed on dividends paid by a locally resident company to a non-resident?

Yes. The domestic withholding tax rate on dividends is 5%.

The Bulgarian withholding tax on dividends may be reduced or eliminated provided a double tax treaty is in force between Bulgaria and the country of residence of the foreign beneficiary of the dividend income.

Dividends paid by a Bulgarian resident company to its parent company resident in another EU-Member State are exempt from Bulgarian withholding tax without any participation or holding period requirements.

### 3.2 Would there be any withholding tax on royalties paid by a local company to a non-resident?

Yes. The withholding tax rate is 10%.

The Bulgarian withholding tax on royalties may be reduced or eliminated provided a double tax treaty is in force between Bulgaria and the country of residence of the foreign beneficiary of royalties.

### 3.3 Would there be any withholding tax on interest paid by a local company to a non-resident?

Yes. The domestic withholding tax rate on interest is 10%.

The Bulgarian withholding tax on interest may be reduced or eliminated provided a double tax treaty is in force between Bulgaria and the country of residence of the foreign beneficiary of the interest income.

### 3.4 Would relief for interest so paid be restricted by reference to "thin capitalisation" rules?

In general, such restrictions do apply in Bulgaria.

### 3.5 If so, is there a "safe harbour" by reference to which tax relief is assured?

Thin capitalisation restrictions are triggered if the debt exceeds three times the equity (i.e. the thin capitalisation safe haven ratio is 1:3).

### 3.6 Would any such "thin capitalisation" rules extend to debt advanced by a third party but guaranteed by a parent company?

Yes, "thin capitalisation" rules apply to debt advanced by a third party but guaranteed by a parent company.

### 3.7 Are there any restrictions on tax relief for interest payments by a local company to a non-resident in addition to any thin capitalisation rules mentioned in questions 3.4-3.6 above?

Deductibility of interest expenses may be disallowed if the interest payment is considered as a hidden distribution of profits. Hidden distribution of profits may exist if at least three of the following conditions are met:

- the debt exceeds the payer's equity as at December 31st of the previous year;
- payment of the debt or of the interest is not limited in time;
- payment of the debt or of the interest, or the interest rates depends on the existence or the amount of the payer's profits; and/or
- payment of the debt depends on other creditors' claims satisfaction or on dividend distribution.

### 3.8 Does Bulgaria have transfer pricing rules?

Yes, it does have transfer pricing rules.

## 4 Tax on Business Operations: General

### 4.1 What is the headline rate of tax on corporate profits?

The corporate income tax rate is 10%.

### 4.2 When is that tax generally payable?

Advance corporate income tax instalments are made either monthly or quarterly depending on the tax result in previous financial years. The final payment of corporate income tax is made by March 31st the following year.

### 4.3 What is the tax base for that tax (profits pursuant to commercial accounts subject to adjustments; other tax base)?

The tax base is the accounting result adjusted for tax purposes in accordance with the rules set out in the Corporate Income Tax Act.

### 4.4 If it otherwise differs from the profit shown in commercial accounts, what are the main other differences?

#### Permanent tax differences

Among others the following expenses shall be deemed permanent

tax differences:

- (a) expenses not related to the business activities;
- (b) expenses improperly documented;
- (c) penalties and other sanctions imposed for violation of the law as well as penalty the interest for unpaid public liabilities; and
- (d) expenses deemed hidden distribution of profits.

#### Temporary tax differences

Among others temporary tax differences include:

- (a) expenses/income from subsequent revaluations of assets;
- (b) provision of liabilities; and
- (c) interest expenses under thin capitalisation regulations.

#### 4.5 Are there any tax grouping rules? Do these allow for relief in Bulgaria for losses of overseas subsidiaries?

Tax grouping rules do not exist.

#### 4.6 Is tax imposed at a different rate upon distributed, as opposed to retained, profits?

The corporate income tax rate does not depend on whether the profits are distributed or retained.

#### 4.7 What other national taxes (excluding those dealt with in "Transaction Taxes", above) are there - e.g. property taxes, etc.?

##### Property Tax

The rate of the property tax varies between 0.05% and 0.2% in the different municipalities.

The property tax is paid in four equal instalments as follows: (i) from February 1st until March 30th; (ii) until June 30th; (iii) until September 30th; and (iv) until November 30th. If the property tax is prepaid in the first period, the tax payer is entitled to a 5% discount.

##### Garbage Fee

The rates of the garbage fee are determined by each municipality.

#### 4.8 Are there any local taxes not dealt with in answers to other questions?

There are also local taxes on inherited properties, on donations, on vehicles, etc.

## 5 Capital Gains

#### 5.1 Is there a special set of rules for taxing capital gains and losses?

##### Bulgarian Companies

Capital gains and losses are taxed under the general corporate income tax rules.

##### Foreign Companies

Foreign companies deriving capital gains from Bulgarian sources are subject to special taxation rules.

#### 5.2 If so, is the rate of tax imposed upon capital gains different from the rate imposed upon business profits?

##### Bulgarian Companies

The tax imposed on capital gains is the same as the tax imposed on business profits.

##### Foreign Companies

The capital gains tax is 10%. If the payer of the capital gains is a Bulgarian company, the tax is withheld from the gain. If the payer of the capital gains is a foreign company, the beneficiary of the gain is liable to pay it to the Bulgarian Budget.

The Bulgarian capital gains tax may be reduced or eliminated if the beneficiary of the gain is resident in a country having a double tax treaty with Bulgaria.

#### 5.3 Is there a participation exemption?

Yes, a participation exemption rule exists with regard to two Bulgarian entities and with regard to a Bulgarian parent company having a subsidiary resident in another EU Member State (no minimum participation or holding period restrictions apply).

#### 5.4 Is there any special relief for reinvestment?

A general relief for reinvestments does not exist.

Bulgarian laws, however, provide for a corporate income tax exemption applicable to production companies investing in regions with high unemployment. One of the conditions for utilisation of the corporate income tax exemption for investments in such underdeveloped regions is related to reinvestments.

## 6 Branch or Subsidiary?

#### 6.1 What taxes (e.g. capital duty) would be imposed upon the formation of a subsidiary?

There are no taxes imposed on the formation of a subsidiary.

#### 6.2 Are there any other significant taxes or fees that would be incurred by a locally formed subsidiary but not by a branch of a non-resident company?

No, there are not.

#### 6.3 How would the taxable profits of a local branch be determined?

A Bulgarian branch would be subject to corporate income tax for profits derived from Bulgaria. Apart from this Bulgarian branches of foreign companies are taxed under rules almost identical to those applicable to Bulgarian companies.

#### 6.4 Would such a branch be subject to a branch profits tax (or other tax limited to branches of non-resident companies)?

There is no branch profits tax as such. A Bulgarian branch of a foreign company shall be subject to a corporate income tax at the rate of 10%.

### 6.5 Would a branch benefit from tax treaty provisions, or some of them?

Generally, the branch may benefit from a treaty provision. There are, however, exceptions that should be examined on a case-by-case basis.

### 6.6 Would any withholding tax or other tax be imposed as the result of a remittance of profits by the branch?

The remittance of branch's profits is not subject to any Bulgarian withholding tax.



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Emil Delchev set up and headed the legal & tax departments of Ernst & Young and Arthur Andersen in the period from 1995 until 2005 when he founded Delchev & Partners. Being 10 years in charge of the tax & legal practices of both Arthur Andersen and Ernst & Young, Emil Delchev brings the most valuable experience in practically all areas of law and taxation. He has guided hundreds of foreign investors in establishing their businesses in Bulgaria in times when Bulgaria changed from state to market economy. He has been involved from both legal and tax perspective in privatisations, restructurings, M&As, due diligence processes and acquisitions. Emil Delchev has provided advice in relation to some of the biggest and most complex transactions in Bulgaria.

## 7 Anti-avoidance

### 7.1 How does Bulgaria address the issue of preventing tax avoidance? For example, is there a general anti-avoidance rule or a disclosure rule imposing a requirement to disclose avoidance schemes in advance of the company's tax return being submitted?

The Bulgarian Corporate Income Tax Act contains rules aimed at prevention of tax avoidance. *Inter alia* the law views the following circumstances as tax avoidance:

- Extension of interest free financing or financing bearing interest differing from market interest.
- Consideration for services that have not been actually rendered.



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Veselina Petkova graduated from Sofia University with two degrees - a Master's degree of Law and a Master's degree of International Relations. Veselina Petkova specialised in taxation and deals with sophisticated tax advice and compliance issues. Her command of English, French, Spanish and Russian has made it possible for her to acquire in-depth knowledge of the European and international aspects of the areas of law she specialises in. Among her colleagues she is known for her industry and ability to provide clear, logical and well-structured arguments in favour of her opinions as well as for her capacity to enshrine the substance of the law in the appropriate legal form.

## Delchev & Partners

law firm

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