

# Asset deal vs share deal

Real estate still represents an interesting opportunity for the business activities of foreign investors. Various types of development projects including commercial centres, administrative buildings or residences are successfully and with substantial gains realised in the Czech Republic. By DITA MALIKOVA and JAROSLAVA TUMOVA, PETERKA&PARTNERS

53

**T**ax matters belong to the fundamental questions that developers should consider before starting the development project. One of the most important covers the method of transferring the project to its purchaser. This transfer may be realised by way of: (i) **asset deal** – i.e. a direct transfer of the ownership right to a real estate asset by means of a sale-purchase contract; (ii) **share deal** – i.e. an indirect transfer of the real estate ownership by means of the acquisition of a share or stocks in the owner of the assets (shares and stocks hereinafter referred to as ‘shares’).

In this article, we would like to highlight the main tax effects of the transactions mentioned above and to summarise their basic tax advantages and disadvantages both for the developer and the purchaser. We have focused solely the situations where the purchaser is a Czech entity/Czech permanent establishment of a foreign entity (‘Czech tax resident’).

## 1. Real estate transfer tax

### 1.1. Asset deal

The transfer of real estate is subject to Real Estate Transfer Tax of 3% in the Czech Republic. The tax base is either the agreed transfer price or the value stipulated in an expert

opinion according to the Czech Valuation Act if this value exceeds the agreed transfer price.

Real Estate Transfer Tax is paid by the seller, while the purchaser is regarded as a guarantor for the tax payment.

### 1.2. Share deal

When using the Share Deal scheme, no real estate is directly transferred and, therefore, no Real Estate Transfer Tax is applied.

## 2. Corporate income tax

### 2.1. Asset deal

Under the provisions of Act Nr. 586/1992, the Income Taxes Act, as amended (‘ITA’), the income from the sale of a real estate asset situated in the Czech Republic to a Czech tax resident is regarded as income from sources in the Czech Republic. Therefore, except for situations where the respective double taxation treaty (‘DTT’) states otherwise, this income is subject to taxation in the Czech Republic.

The corporate income tax base is calculated as the difference between the taxable income from the sale of the real estate asset (i.e. its sale price) and its residual value<sup>1</sup>. This difference is to be declared in the annual Czech Corporate Income Tax Return of the seller, regardless of whether it is a company seated in

Czech Republic or not.

Losses incurred in connection with the transfer of real estate may be deducted from the corporate income tax base. However, it is not possible to realise a tax deductible loss from the transfer of a plot of land. Therefore, the purchase price should always be divided into the part relating to buildings and the part relating to land plots.

### 2.2. Share deal

**a) Parent company transferring the share is seated in the Czech Republic**  
If the seller of a share in a Czech company is a Czech tax resident, the income thus received is subject to Czech Corporate Income Tax.

The tax base is calculated as the difference between the taxable income of the parent company earned from the sale of a share (i.e. the sale price) and its purchase price (i.e. the amount of the paid-up capital or the acquisition price of the share in the case of its acquisition).

Any eventual loss incurred from the transfer of a share cannot be deducted from the tax base of the seller.

**b) Parent company transferring the share is seated outside the Czech Republic**

If the seller of a share in a Czech company is a parent company seated outside the Czech Republic and the purchaser is a Czech tax

resident, the related income is taxable in the Czech Republic<sup>2</sup>. However, the above principle is applied only if the relevant DTT does not state otherwise.

In this regard, DTTs may contain the following alternatives:

(i) Income is taxable in the state of the tax residence of the parent company – this provision is included in the majority of DTTs.

(ii) Income is taxable in the Czech Republic – i.e. the income is subject to taxation in the purchaser’s residence state or, in the case of companies whose assets are formed mainly from real estate, the state in which the real estate is situated.

If the income is subject to taxation in the Czech Republic it is taxed via the filing of the Corporate Income Tax Return of the seller<sup>3</sup>.

Double taxation of the above income is avoided in compliance with the method stipulated by the respective DTT.

## 3. Value added tax (‘VAT’)

### 3.1. Asset deal

Pursuant to Act Nr. 233/2004, the Value Added Tax Act, as amended, the supply of real estate situated in the Czech Republic is considered as a supply of goods with the place of supply in the Czech Republic and, therefore, the Czech VAT Act applies.

Generally, the supply of buildings is regarded as a

<sup>1</sup>The residual value of real estate is the purchase price of the respective real estate (i.e. expenses incurred in connection with the construction of a building and/or the acquisition of a plot of land) reduced by the amount of depreciation, if any.

<sup>2</sup>If both the seller and the purchaser are Czech tax non-residents, the income from the sale of a share is not considered as an income with its source in the Czech Republic and Czech

Corporate Income Tax should not be applied. Again, this principle applies unless the relevant DTT stipulates otherwise.

<sup>3</sup>If the seller is not a tax resident of an EU or EEA member state, a Czech purchaser is obliged to withhold tax securement for the respective Czech tax.

54

taxable supply, whilst the supply of plots of land is VAT exempt. However, there exist certain exceptions to this rule:

- (i) The supply of structures, flats and non-residential premises or their part is VAT exempt after the expiry of three years from their acquisition or approval for use (one condition is sufficient).
- (ii) The transfer of building plots of land is regarded as a taxable supply. A 'building plot of land' means an unbuilt<sup>4</sup> plot of land on which a structure connected to the ground by

firm foundations may be constructed in accordance with the relevant building permission.

### 3.2. Share deal

If the seller (parent company) has its seat in the Czech Republic, the Czech VAT Act is applicable to the sale of shares. According to this Act, a transfer of shares is not considered as a taxable supply and thus is not subject to Czech VAT.

If the parent company is seated outside the Czech Republic the tax legislation of the state of its residence applies.

### Conclusion

With regard to the above, it is obvious that Developers will generally prefer a Share Deal as its tax treatment is more advantageous for them than in the case of an Asset Deal.

In an Asset Deal, developers may theoretically face the risk of double taxation (taxation of the income from the sale and of the dividends subsequently distributed to the parent company). This risk may be avoided in the case where the EU Parent-Subsidiary Directive<sup>5</sup> applies or if the respective DTT stipulates a zero tax

rate on dividends.

Purchasers will usually prefer an Asset Deal, where they don't face a risk of inheriting unknown liabilities of the company purchased.

Moreover, if the purchaser acquires the asset directly, its full purchase price may be used as the basis for depreciation and, thereby, additional tax savings may be generated. ■

*Please note that the above article is for information only. Should you wish for more comprehensive information please do not hesitate to contact us.*

<sup>4</sup> An unbuilt plot of land shall be a plot of land on which there is no structure which is regarded as a thing.

<sup>5</sup> 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



**PETERKA & PARTNERS**

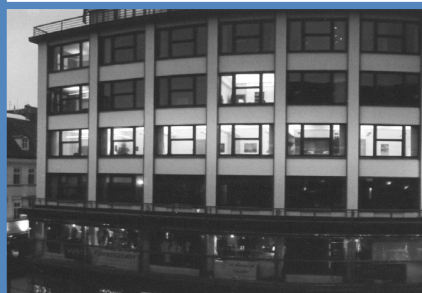
Advokátní kancelář, Law Offices, Cabinet of lawyers

## DRIVING YOUR BUSINESS FORWARD

**Real Estate & Construction • Mergers & Acquisitions • Litigation & Arbitration**

**Corporate & General Commercial • Banking & Finance**

**IP & IT • Labour Law • Bankruptcy Proceedings • EU Law • Tax Law**



P R A G U E

B R A T I S L A V A

K Y I V

**www.peterkpartners.com**