

The Impact of the COVID-19 Pandemic on the Possibilities of Deducting Tax Losses in the Conditions of the Slovak Republic

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Abstract: *One of the tools for optimizing the tax base or an opportunity to reduce the tax burden on taxable persons is the deduction of tax loss. This is a tax loss that the taxpayer has reported in previous tax periods, and there are precise rules for deduction. These rules are set by Act no. 595/2003 Coll. on income tax, as amended, and in recent years there have been several changes to the rules for amortization of tax loss. A significant adjustment of these rules took place during 2020, when Act no. 67/2020 Coll. on certain emergency financial measures in connection with the spread of the dangerous human disease COVID-19, as amended, and amending certain laws (hereinafter referred to as "Lex Korona"). The rules adopted during the COVID-19 pandemic enabled taxpayers to apply a significantly larger part of tax losses accumulated in the years 2015 to 2018 when calculating the tax base already in 2019. In the article we will focus on the rules and procedures for deducting tax losses in the period until 31. December 2019, during the COVID-19 pandemic period and new rules effective from 1. January 2020.*

Keywords: Tax losses, Tax base, Lex Korona

JEL codes: H25, K34

1 Introduction

Tax loss is the difference by which tax expenses exceed taxable income while respecting the material and temporal connection of taxable income and tax expenses in the relevant tax period (Article 2 letter k), Act No. 595/2003 Coll. on Income Tax as later amended). The rules for deducting tax loss are set out in Section 30 of this Act. In order to mitigate the consequences of the COVID-19 pandemic, the provision of Article 24b (1) "Lex Korona", which allowed taxpayers to choose an alternative procedure for deducting tax loss during the COVID-19 pandemic.

The vast majority of entities to which the possibility of deducting tax losses applies are business entities. For the sake of completeness, it should be noted that this option also applies in certain cases to entities that are primarily established for the purpose of performing a non-profit activity (Kordošová, 2016). Budgetary and contributory organizations as well as municipalities, in addition to income from the main activity, which are exempt from tax (Article 13 (1) letter a), Act No. 595/2003 Coll. on Income Tax as later amended), may also achieve income from business activities, which are subject to taxation. This income and the related expenses are included in the tax base, from which it is possible to deduct tax losses incurred in previous tax periods under the same conditions as apply to legal and natural persons carrying out business activities.

A tax loss cannot be reported by a natural person who applies expenses to business income as a percentage of income, and a natural person, even if he claims demonstrable expenses, but achieves income in accordance with Act No. 595/2003 Coll. on Income Tax as later amended: Income from Employment (Article 5), Income from leasing (real estate) (Article 6 (3)), Income from the use of a work and from the use of artistic performance (Article 6 (4)), Income from capital property (Article 7) or other income (Article 8).

2 Methodology and Data

Basic rules valid until 31. December 2019:

From the tax base of a taxpayer who is a legal entity, or from the tax base (partial tax base) on income according to Article 6 (1) and (2) of a taxpayer who is a natural person, a tax loss may be deducted evenly over four consecutive tax periods, beginning with the tax period immediately following the tax period for which the tax loss was recognized. On the day of the taxpayer's entry into liquidation or declaration of bankruptcy, the right to deduct the tax loss from the date of entry into liquidation or declaration of bankruptcy expires. If the tax period is less than a year, the taxpayer can claim the full annual deduction of tax loss.

If the taxpayer who started deducting the tax loss ceased to exist as a result of the cancellation without liquidation, the tax loss is deducted by the legal successor. In the event that there are more legal successors, the tax loss is deducted for each of them proportionally, according to the amount of equity of the defunct taxpayer, in which it passed to the individual legal successors. The legal successor may deduct a tax loss if the merging legal entity and its legal successor are taxpayers of corporate income tax and at the same time if the purpose of such termination is not only to reduce or avoid tax liability.

Temporary rules under "Lex Korona":

The provision of Article 24b (1) "Lex Korona" allowed unclaimed tax losses reported under a special regulation for tax periods ended in 2015 - 2018 to be deducted from the income tax base by a corporate taxpayer or to be deducted from the income tax base (partial income tax base) from the income taxpayer, which is a natural person, if the last day of the deadline for filing an income tax return for the tax period expires in the period from 1. January 2020 to 31. December 2020. The limit set in "Lex Korona" was the maximum possible amount of tax deductible losses **totaling up to EUR 1 000 000**. All other restrictive conditions have been temporarily repealed by the relevant provision.

Basic rules valid from 1. January 2020:

The tax loss can be deducted from the tax base of a taxpayer who is a legal entity, or from the tax base (partial tax base) on income according to Article 6 para. 1 and 2 of a taxpayer who is a natural person, for a maximum of **five consecutive tax periods**, starting with the tax period immediately following the tax period for which the tax loss was recognized. The taxpayer may apply this deduction of tax loss **up to the amount of the tax base** of the taxpayer who is a legal entity or the tax base (partial tax base) on income according to Article 6 (1) and (2) of a taxpayer who is a natural person if they are considered as **micro-taxpayers** in the relevant tax period in which they claim a tax loss deduction. If the taxpayer **does not meet the criteria of a micro-taxpayer**, he can claim a deduction of tax loss **up to a maximum of 50% of the achieved tax base**.

If the taxpayer who started deducting the tax loss ceased to exist as a result of the cancellation without liquidation, the tax loss will be deducted by the legal successor. If there are several legal successors, the tax loss is deducted on the part of each of them proportionally, according to the amount of the registered capital of the dissolved taxpayer transferred to the individual legal successors. A legal successor may deduct a tax loss if the legal person has ceased to exist and its legal successor is a corporate taxpayer and provided that the purpose of such cancellation is not merely to reduce or avoid tax. On the day of the taxpayer's entry into the liquidation or bankruptcy order, the taxpayer's right to deduct the tax loss expires on the day of entry into the liquidation or bankruptcy order. If the tax period is shorter than 12 consecutive calendar months, the taxpayer may claim the full annual deduction of tax loss.

3 Results and Discussion

Based on the above rules of deduction of tax loss in the following tables, we present simulations of how the individual methodologies would affect the tax burden of tax subjects. For comparability, we use the simulations from the same starting situation t. from. the taxable entity has achieved the same results in six consecutive tax periods (tax loss / tax base) and the same tax rate of 21 % is applied in all periods. In the individual simulations, the rules used to deduct the tax loss are as follows: Table 1 contains the procedure according to the basic rules valid until 31. December 2019, it means, simulation of the situation, if there were no change in the legislation as of 1. January 2020. Table 2 shows the simulation of the status of deduction of tax loss according to the rules valid from 1. January 2020 and Table 3 shows the simulation of the procedure allowed by the temporary legislation based on "Lex Korona".

Table 1 Deduction of tax loss – basic rules valid until 31. 12. 2019

Period	Year 1 (2016)	Year 2 (2017)	Year 3 (2018)	Year 4 (2019)	Year 5 (2020)	Year 6 (2021)	Total
Tax loss (TL)	75 000,00	X	X	X	X	X	X
1/4 TL	18 750,00	X	X	X	X	X	X
Tax base (TB)	X	9 000,00	27 000,00	96 000,00	0,00	3 000,00	X
TL deducted	X	9 000,00	18 750,00	18 750,00	0,00	X	46 500,00
TL not deducted	X	9 750,00	0,00	0,00	18 750,00	X	28 500,00
TL remaining	X	56 250,00	37 500,00	18 750,00	0,00	X	X
TB adjusted	X	0,00	8 250,00	77 250,00	0,00	3 000,00	X
Tax (21 %)	X	0,00	1 732,50	16 222,50	0,00	630,00	18 585,00

Source: own processing

According to the simulation in Table 1, we can conclude that from the total tax loss reported in year 1 (2016) in the amount of EUR 75 000,00, the taxpayer could deduct the amount of EUR 46 500,00 during the statutory period of 4 years, which means that he will never be able to use the value of the tax loss of EUR 28 500,00 to reduce his tax liability. The total amount of tax paid by the tax subject for the observed period is EUR 18 585,00.

Table 2 Deduction of tax loss - basic rules valid from 1. 1. 2020

Period	Year 1 (2020)	Year 2 (2021)	Year 3 (2022)	Year 4 (2023)	Year 5 (2024)	Year 6 (2025)	Total
Tax loss (TL)	75 000,00	X	X	X	X	X	X
1/4 TL	X	X	X	X	X	X	X
Tax base (TB)	X	9 000,00	27 000,00	96 000,00	0,00	3 000,00	X
50 % TB	X	4 500,00	13 500,00	48 000,00	0,00	1 500,00	X
TL deducted	X	4 500,00	13 500,00	48 000,00	0,00	1 500,00	67 500,00
TL not deducted	X	X	X	X	X	X	7 500,00
TL remaining	X	70 500,00	57 000,00	9 000,00	9 000,00	7 500,00	X
TB adjusted	X	4 500,00	13 500,00	48 000,00	0,00	1 500,00	X
Tax (21 %)	X	945,00	2 835,00	10 080,00	0,00	315,00	14 175,00

Source: own processing

Based on the simulation in Table 2, we can state that from the total tax loss reported in year 1 (2020) in the amount of EUR 75 000,00, the tax entity could deduct the amount of EUR 67 500,00 during the statutory period of 5 years, which means that he will never be able to use the value of the tax loss of EUR 7 500,00 to reduce his tax liability. The total amount of tax that the taxpayer will pay for the observed period is EUR 14 175,00. Compared to the rules in force until 31. December 2019, the new legislation brought a positive change in the area of deduction of tax loss, as the tax burden of the subject in the simulated situation decreased by EUR 4 410,00, which corresponds to a tax loss of EUR 21 000,00 (TL not deducted: 28 500,00 – 7 500,00) by which more was deducted from the tax base in the second simulation.

Table 3 Deduction of tax loss - temporary rules according to „Lex Korona“

Period	Year 1 (2016)	Year 2 (2017)	Year 3 (2018)	Year 4 (2019)	Year 5 (2020)	Year 6 (2021)	Total
Tax loss (TL)	75 000,00	X	x	X	x	X	X
¼ TL	18 750,00	X	X	x	X	x	X
Tax base (TB)	X	9 000,00	27 000,00	96 000,00	0,00	3 000,00	X
TL deducted	X	9 000,00	18 750,00	37 500,00	X	X	65 250,00
TL not deducted	X	9 750,00	0,00	0,00	X	X	9 750,00
TL remaining	X	56 250,00	37 500,00	0,00	X	X	X
TB adjusted	X	0,00	8 250,00	58 500,00	0,00	3 000,00	X
Tax (21 %)	X	0,00	1 732,50	12 285,00	0,00	630,00	14 647,50

Source: own processing

The simulation in Table 3 shows the possibility of deducting the tax loss according to the rules that were temporarily adopted on the basis of the "Lex Korona". Under that provision, it was possible to deduct accumulated tax losses not yet deducted from the tax base achieved for the tax period year 2019. In the simulation, this is a one-time deduction of a tax loss in the amount of EUR 37 500,00. Compared to the simulation in Table 1, it is clear that the COVID-19 pandemic mitigation measure reduced the taxpayer's tax burden by EUR 3 937,50 (Tax: 12 285,00 – 16 222,50).

Conclusions

Given the rules, which have changed several times in a relatively short time and require input data on tax losses from several previous tax periods and also have an impact on several subsequent tax periods, it is relatively difficult to navigate the issue of deducting tax losses. With effect from 1. January 2020, the method of deducting tax loss has changed. This new method of deducting the tax loss will be applied for the first time to the tax loss reported for 2020. The tax loss reported for 2020 may be deducted unevenly by the taxpayer for five consecutive tax periods, starting in 2021. The taxpayer may claim this deduction for tax loss. up to a maximum of 50% of the tax base (partial tax base) on income from business and other self-employed activity reported for 2021. Tax losses reported for the years 2017 to 2019 can be deducted from the tax base in a manner valid until 31.12.2019 in the amount of ¼.

Changing legislative conditions require accounting experts, whether in the position of accountants, financial managers or employees of specialized companies that are engaged in the provision of accounting services and tax advice in a so-called supplier way. "Outsourcing of Economic Activities" (Meluchová, Mateášová, 2017), constant monitoring of changes in order to make the most effective use of opportunities to reduce the tax burden on taxpayers. In addition to accounting, such correct decisions as in the valuation or selection of a valuation variable (Juhászová, Markovič, Mokošová, 2014), it is necessary to do in the field of taxation, which is not possible without timely and correct information.

It should also be noted that the rate of reduction of the tax burden due to the possibility of deducting a tax loss depends to a large extent on the results (achieved tax bases) of the taxable person in the periods during which the deduction of tax loss is possible. It is therefore not possible to conclude that these changes will be for each taxpayer represent a saving of funds.

Acknowledgments

This paper has been supported by the VEGA project 1/0121/21 "The Analysis of Impact of Crises Related to COVID-19 on Financial Health of Entities in the Slovak Republic".

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