

Trends in tax inspections

Bosnia and Herzegovina
November 2019



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Introduction

Both the business environment and the tax authorities seek, or should seek, to ensure a tax administration process as balanced and flexible as possible - a taxpayer-supportive process that will not disrupt their businesses while providing protection throughout the proceedings. It is for this reason that the tax inspections conducted by the Indirect Taxation Authority and Tax Authorities in both entities are a topic of constant debate, with legislation amendment proposals aimed at streamlining the ITA and TA - taxpayer relationship.

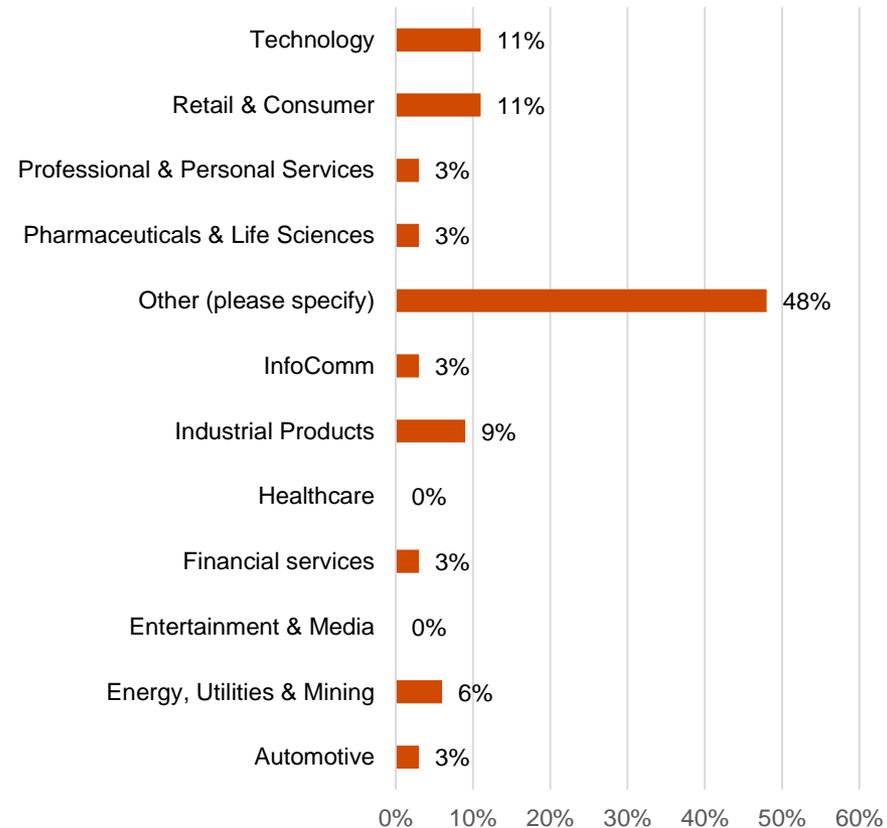
To provide an overview of the tax inspection trends in Bosnia and Herzegovina, we conducted our first survey in 2019, with 35 companies operating in Bosnia and Herzegovina as respondents. Its results were greatly appreciated by the business environment. In light of the positive response to our survey in other CEE countries, we have produced edition for Bosnia and Herzegovina with recommendations and conclusions. Our primary focus was to find out and analyze information on tax inspections, namely their frequency, duration and effects, the main aspects examined by inspection teams, the number of respondents that chose to challenge tax assessment documents, the outcome of those appeals and other elements detailed in this presentation.

Survey Respondents

In what industry does your business operate?

The 35 companies participated in this survey, operating in various industries, such as retail & consumer and technology (both with 11%), industrial products (9%), energy, utilities & mining (6%) and the following industries each with (3%): automotive, financial services, info-comm, pharmaceuticals & life sciences and professional & personal services.

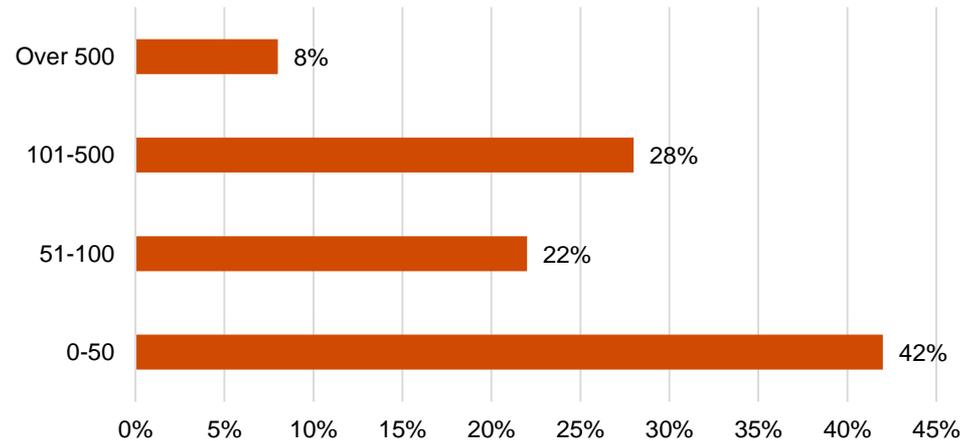
The (48%) from the survey respondents are from various other sectors, such as real estate, wholesale, food industry, construction industry, chemical industry, production and distribution of technical and medical gases and related equipment etc.



Survey Respondents

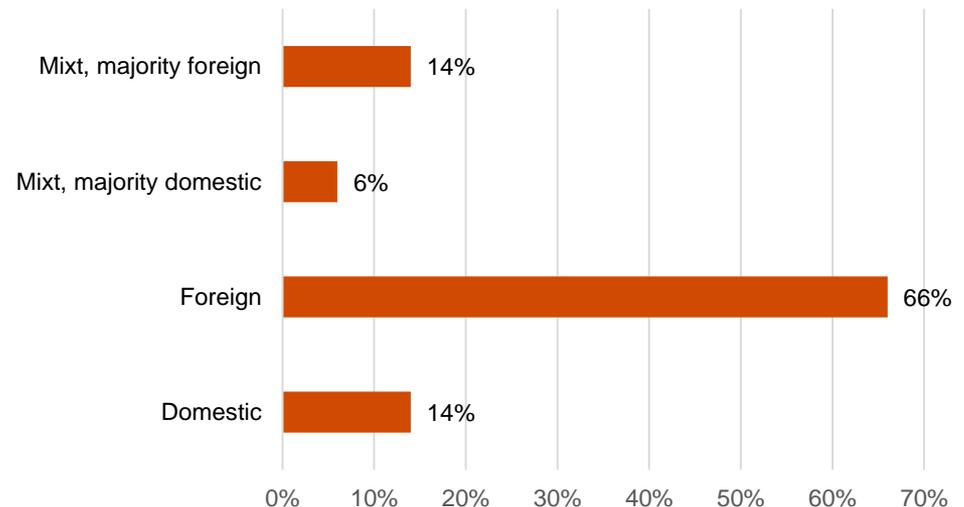
What is your company's headcount?

According to our survey results, more companies (42%) had up to 50 employees than were in any other headcount bracket, followed by those with a headcount between 101 and 500 employees (28%). Businesses with a headcount between 51 and 100 account for (22%) of the respondents, and those with a headcount over 500, for (8%).



What source does your company's capital have?

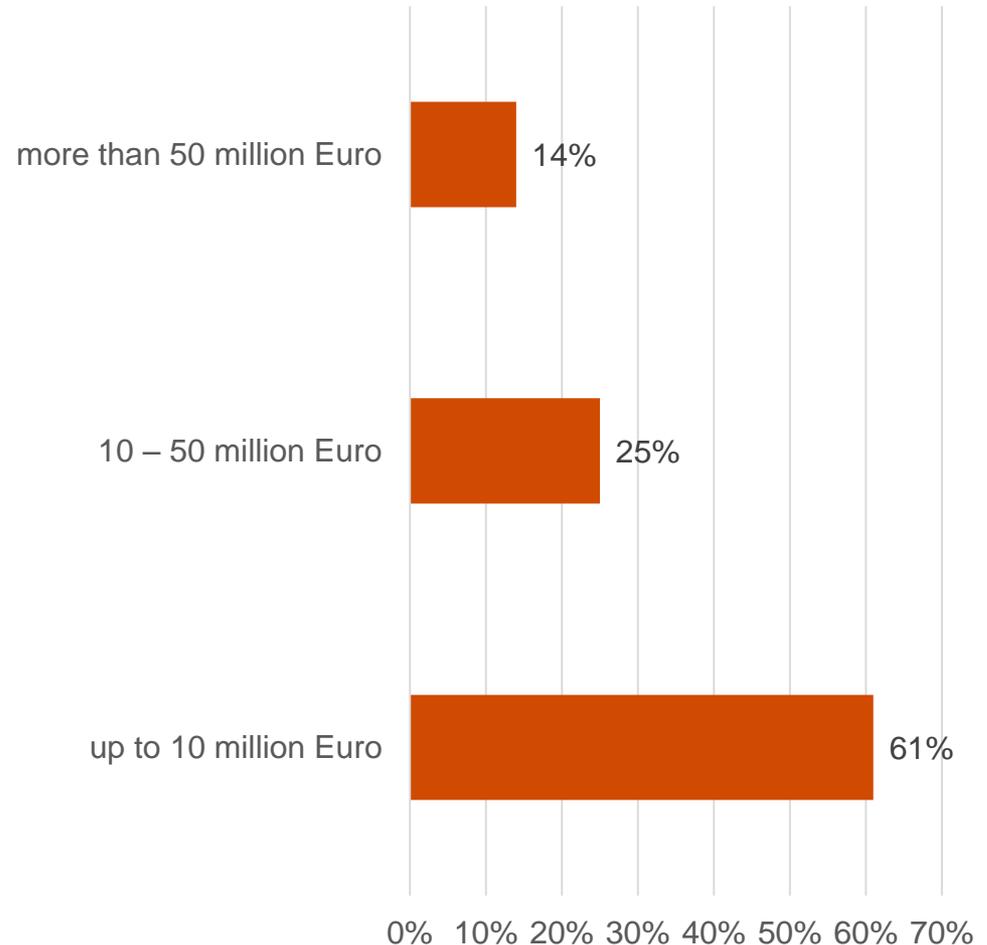
From the perspective of the capital source of the survey respondents, the majority (66%) of the companies have foreign capital and (14%) have a domestic one. 20% of the respondents represent companies with a mixt capital, majority foreign (14%), while (6%) represent companies with a mixt capital, majority domestic.



Survey Respondents

What is the turnover of your company?

Almost two thirds of the survey respondents (61%) are from companies with a turnover of up to EUR 10 million and operating mainly in energy, utilities & mining, financial services, pharmaceutical & life sciences, professional and personal services and technology sectors. (25%) of the respondents are from companies with a turnover between EUR 10 and EUR 50 million, 26% operating mainly in automotive and industrial products sectors and (14%) from companies with a turnover over EUR 50 million from info-comm companies.



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What does

the official

data say?

Tax inspections

What does the official data say?

Statistics reports posted on Indirect Taxation Authority website show that the number of tax inspections for the 2018 was lower than the figure for the same period of 2017. There is an increase in the number of full tax inspections, by almost 21.36% in 2018 when compared to the 2017 figure. Total gross effects, i.e. additional tax liabilities assessed under inspector's decisions in controls are 2.98% higher in 2018 comparing to the 2017 figure.

Indirect Taxation Authority		
Indicator	2018	2017
Number of tax inspections	7,322	8,816
Number of full indirect tax inspections	5,141	4,236
Additional tax liabilities assessed	67,789,609	65,830,758
Number of subsequent custom inspections	847	924
Additional custom liabilities assessed	2,455,671	944,089

Tax inspections

Statistics reports posted on Tax Administration of Republic of Srpska website show that the number of tax inspections for 2018 was lower than the figure for the same period of 2017. There is an increase in the number of special additional tax inspections, by 2.89% in 2018 when compared to the 2017 figure. A significant decrease in the additional tax liabilities assessed is noticeable, by almost 35% in 2018 comparing to the 2017 figure.

Statistics reports posted on Tax Administration of the Federation of Bosnia and Herzegovina website show that the number of tax inspections for 2018 was lower than the figure for the same period of 2017. A significant increase in the number of special additional inspections (“fast inspections”) is noticeable, by almost 34 % in 2018 when compared to the 2017 figure. However, there is decrease of additional tax liabilities assessed at the approximate amount of 15 million BAM that is 5.82% lower in 2018 comparing to 2017.

Tax Administration of Republic of Srpska		
Indicator	2018	2017
Number of tax inspections	3,454	3,922
Additional tax liabilities assessed	about 2% of the total paid direct taxes liabilities	
Special additional inspections	3,625	3,520

Tax Administration of FBiH		
Indicator	2018	2017
Number of tax inspections	6,485	6,575
Additional tax liabilities assessed	about 5% of the total paid direct taxes liabilities	
Special additional inspections	16,196	12,081



In Bosnia and Herzegovina, there are 37,587 registered active enterprises. This data does not cover entrepreneurs (natural persons conducting an economic activity). Quality and scope of available data on them are still not reliable enough for publication. During the 2018, ITA, TA RS and TA FBiH conducted 19,313 different inspections in total.

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What does

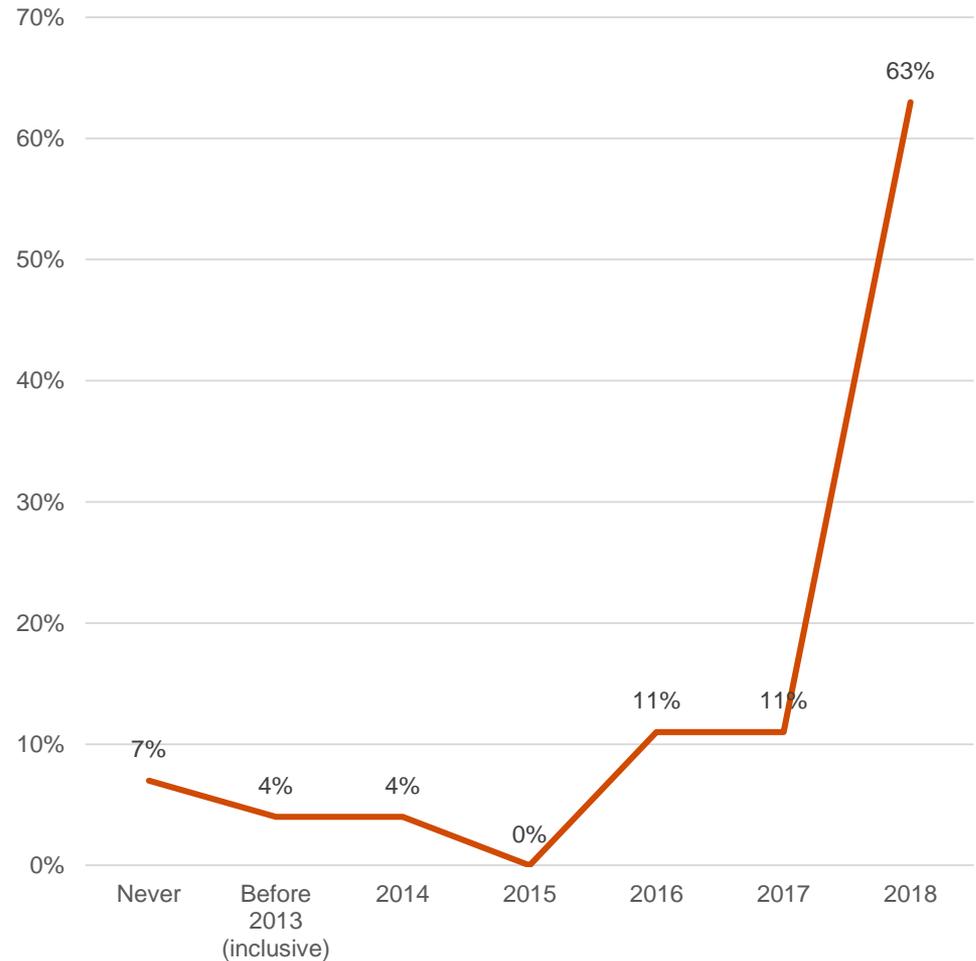
the survey

data say?

What does the survey data say?

When were you last subject to a tax inspection?

The survey results show that before 2013 tax inspections were conducted at one respondent. An increase is noticeable in the number of tax inspections conducted in 2018 (63% of the respondents) compared with 2017 (11% of respondents). In the other years, 2014 to 2017, the percentage of respondents inspected was ranging between (4%) and (11%) of the total. It is noteworthy that only (7%) of the respondents were not subject to tax inspections during this six-year period. The main aspects to be examined by tax inspectors during these inspections are combatting profit shifting, looking into how large companies manage economic intra-group relationships and dismantling transaction chains devised to circumvent compliance with tax requirements, by detecting and prosecuting tax fraud cases that have a significant adverse effect on the state budget.

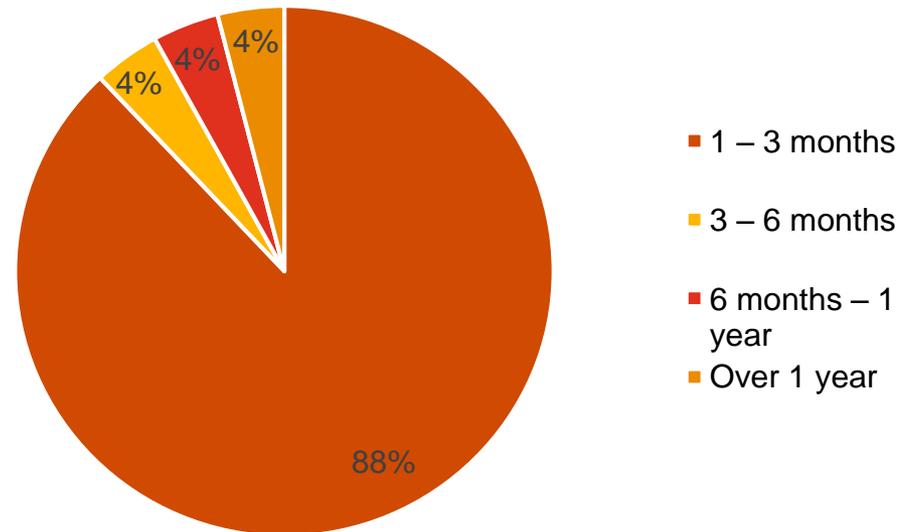


What does the survey data say?

How long did the latest inspection last?

For 88% of the respondents the actual duration of a tax inspection was up to three months. In 12% of the cases, the actual duration of an inspection was longer than six months (even longer than one year in 4% of the cases). According to legal provisions, tax inspections should be conducted in a way that will not disrupt the day- to-day business of companies, allowing them to focus on generating added value that will entail growth for the business and job creation. It should also be noted that other countries encourage electronic inspections conducted by means of SAF-T standard forms.

Additionally, 62% respondents noted that company's activities were affected as a result of tax inspections. Reasons for this being duration of the tax inspections, amount of information and combination of duration and amount of information.



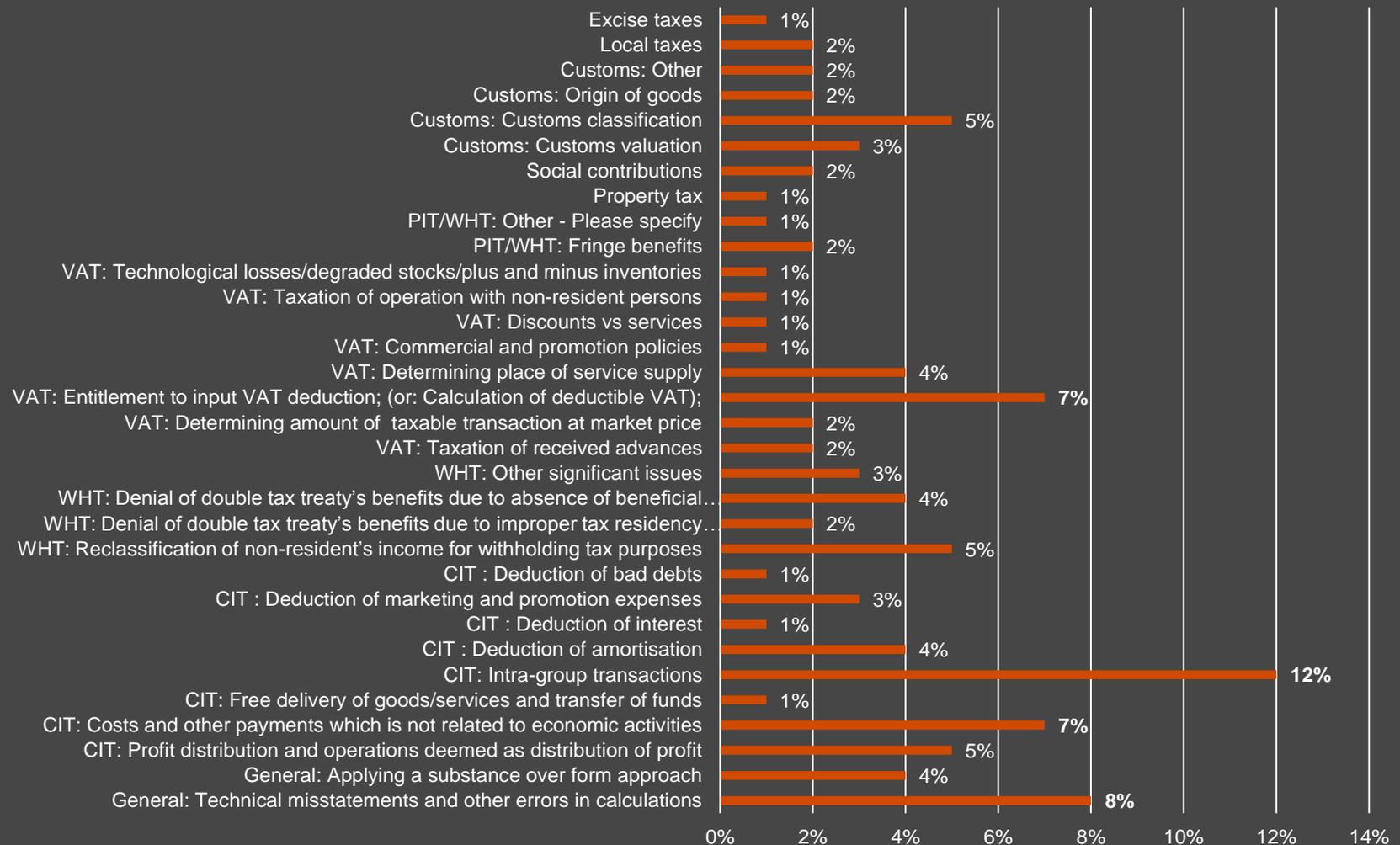
What does the survey data say?

What are the main aspects identified during tax inspections?

The survey results show that tax inspection teams mainly focused on the following aspects:

- **Corporate Income Tax (CIT)**, as indicated by 34% of respondents mainly from companies operating in retail & consumer, energy, utilities & mining, industrial products and info-comm sectors. Under corporate income tax, the most common aspects pertained to the intra-group transactions (12%), costs and other payments that are not related to economic activities (7%), the profit distribution and operations deemed as distribution of profit (5%) deductibility of amortization (4%), the deductibility of marketing and promotion expenses (3%), deduction of bad debts (1%).
- **Value Added Tax (VAT)**, as indicated by 19% of respondents mainly from companies operating in automotive, industrial products and pharmaceutical & life sciences sectors. The entitlement to input VAT deduction was indicated as being the most frequently targeted aspect (7%). Respondents also named the VAT implications resulting from determining place of service supply (4%), from determining the amount of taxable transaction at market price (2%), from taxation of received advances (2%) and from other topics (4%).
- **Withholding Tax (WHT)**, indicated by 14% of the respondents from companies operating mainly in retail & consumer, energy, utilities & mining and financial sectors. The most targeted topics under this section were the reclassification of non-resident's income (5%), the denial of double tax treaty's benefits due to absence of beneficial ownership of income paid/payable to a non-resident (4%), the denial of double tax treaty's benefits due to improper tax residency certificate of a non-resident or other formalities (2%) and other related topics (3%).
- **General aspects** indicated by 12% of the respondents from different industries, with the technical misstatements and other errors in calculations being the most targeted one (8%). Another aspect indicated was the analysis of the substance over the form of economic transactions (4%).
- **Other aspects** pertained mainly to customs issues (12%), PIT/WHT issues (3%), social contributions (2%), local taxes (2%), excise tax (1%), property tax (1%).

What does the survey data say?

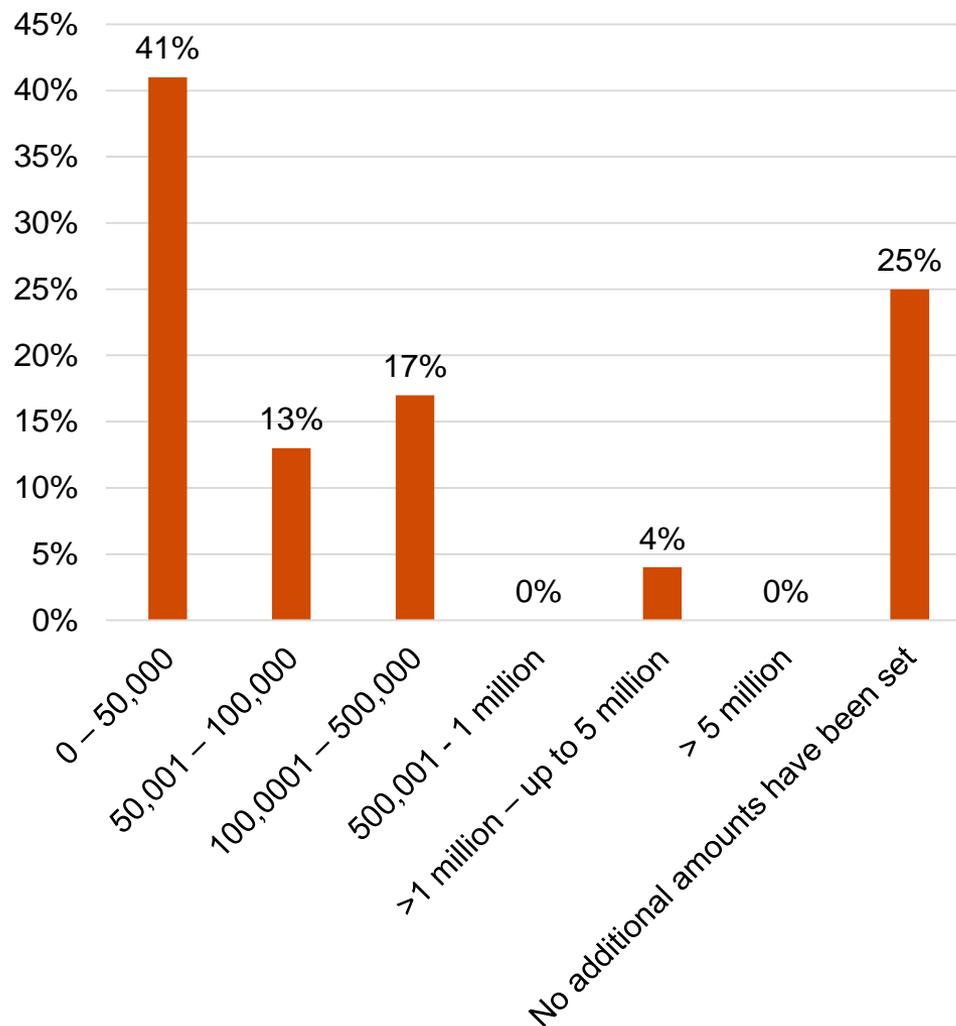


What does the survey data say?

What was the figure of additional amounts assessed following tax inspections?

Additional amounts assessed as due by taxpayers vary substantially. It is noteworthy that in (25%) of the cases no additional liabilities were assessed following tax inspections. In (41%) of the cases, additional liabilities assessed by tax inspectors were lower than BAM 50,000 (approximately EUR 25,000). Between these two extremes there were cases where the additional amounts assessed ranged between BAM 50,000 and 100,000 (13%), BAM 100,000 and 500,000 (17%), BAM 500,000 and 1 million (0%), BAM 1 million and 5 million (4%) or above BAM 5 million (0%).

Our experience shows that with most tax inspections there are aspects challenged by the tax authorities, but some of them are clarified as early as the on-site stage of inspections, as taxpayers come up with explanations and produce documents that clear things up for tax inspectors.



What does the survey data say?

46%

Yes

54%

No

Appeals against tax assessment documents

More than half of our respondents, 54%, chose not to appeal against the tax assessment documents issued following tax inspections. The main reason for the high number of businesses deciding not to challenge tax assessment documents is the tax inspection findings have been accepted (77%) answers. Other reasons are small number of findings, distrust in the effectiveness of the challenge and other reasons.

The companies that appealed operate in following industries: Energy, Utilities & Mining, Financial services, Industrial Products, Retail & Consumer and Other Industry.

The companies that didn't appeal operate in following industries: Automotive, Info-comm, Pharmaceutical and Life Sciences, Technology.

What does the survey data say?

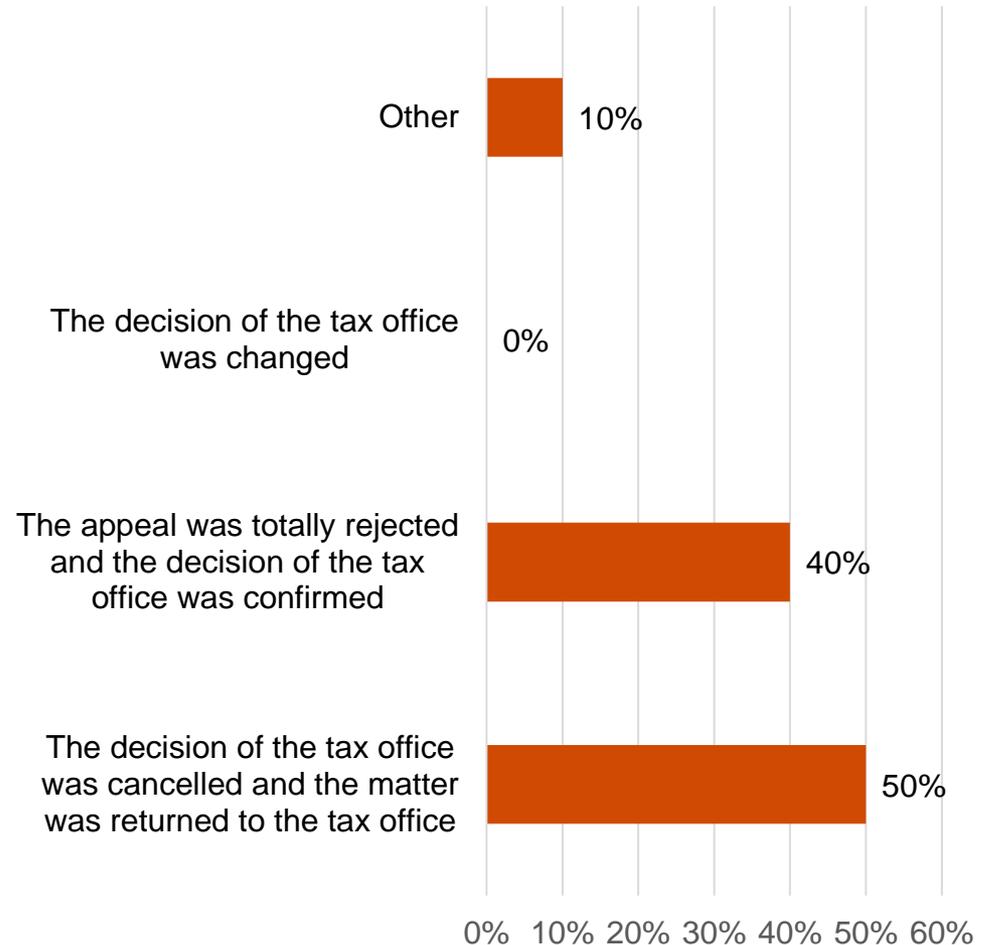
How was the appeal solved by the appellate body?

Where businesses challenged the tax assessment documents, (50%) were issued settlements annulling in full or in part the tax assessment documents, and matter was returned to the tax office.

The settlements favorable to the taxpayers (0%), go to show that there is still a restrictive interpretation of tax legislation by tax inspectors.

For (40%) of the cases the appeals were rejected in full.

For (10%) of the cases the appeals are most often still pending or the tax inspection report conclusions are still under discussion.



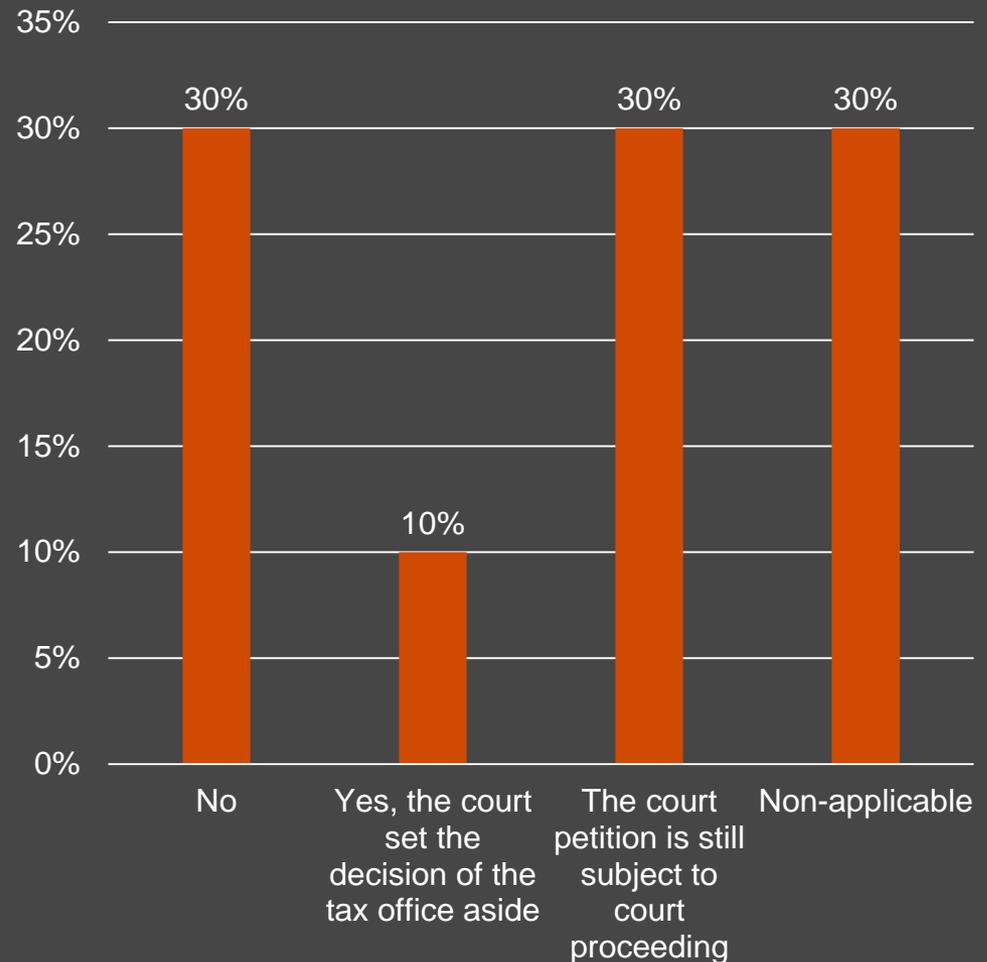
What does the survey data say

If the solution to the above appeal was negative did you appeal to court proceedings?

Of those that were issued a negative or partly favorable settlement to appeals against tax assessment documents, a (30%) chose to challenge the tax assessment documents in court.

For approximately (10%) of the taxpayers that chose to take legal action, the court ruled to set the decision of the tax office aside. For the other cases (30%), the file is still pending in court.

For (30%) of the respondents the appeal settlement proceedings are still under way, with a decision on whether to take their case further to court to be made after the appeal settlement result has been issued, and depending on it.



What does the survey data say?

Have you been assisted by an external tax and/or legal advisor during or after the tax inspection?

Half of the respondents (50%) turned to external advisors during or after the completion of the tax inspection, whereas the other half (50%) did not use the services of external advisors.

Half of the respondents (50%) used the external advisor during the tax inspection process, (17%) during the tax dispute procedures and (33%) respondents asked for external advisor services before the tax authority initiated the tax inspection.

Respondents said YES for using external tax and/or legal advisor during or after tax inspection.

50%

Additional findings

Aassistance or clarifications from the tax authorities

According to our survey results, more than three thirds of respondents (69%) from all industries requested assistance or clarifications from the tax authorities.

As per the survey results, the respondents used several ways to contact authorities for asking assistance, such as:

- either by a letter, indicated by (38%) of respondents mainly from industrial products, info-comm and technology sectors, and
- by Call Center, as indicated by (34%) of respondents mainly from automotive, energy, utilities & mining and retail & consumer, and
- by e-mail, indicated by (28%) of respondents mainly from infocomm, pharmaceutical & life sciences and technology sectors.

Areas in the activity of tax authorities that generate discontent

As per the survey results, areas in the activity of tax authorities that generate discontent for the survey respondents vary a lot. The most frequently mentioned are the following:

- long deadlines for solving/answering to our inquiries, by 25% of the respondents,
- lack of accountability and integrity of the tax officers, by 18% of the respondents,
- call center/assistance services, by 17% of the respondents,
- the extended duration of tax inspections, by 13% of the respondents,
- (27%) other as a subjective interpretation of regulations, limited functionality of Virtual Private Space (e-account), appeal procedures, other on-distance forms of control etc.

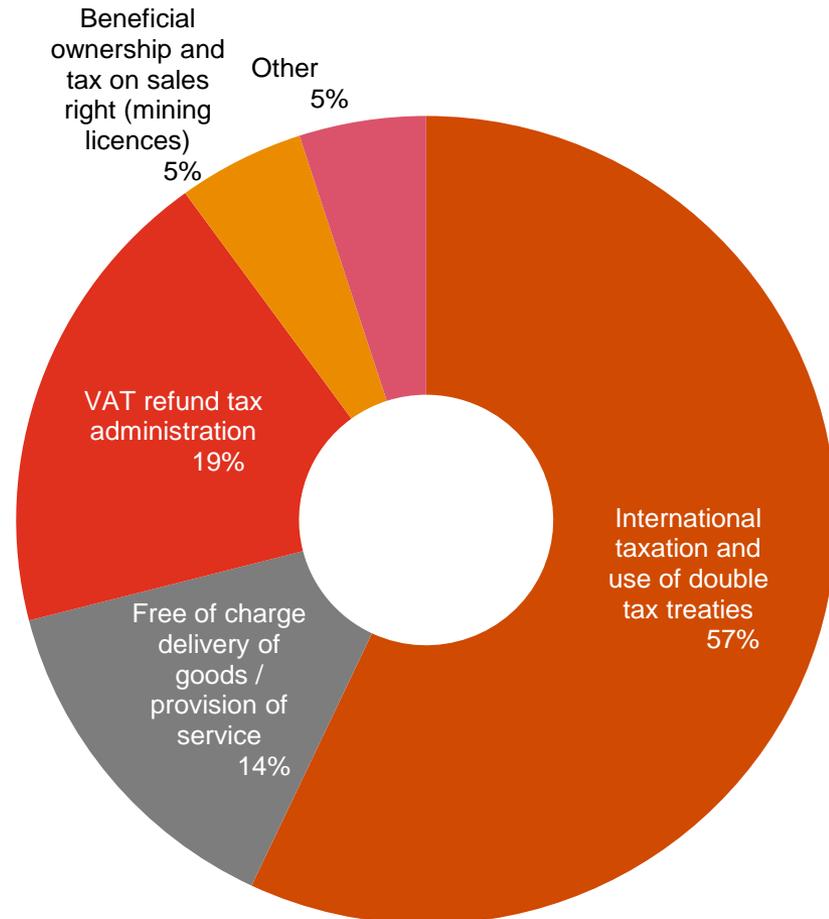
Additional findings

Lack of clarity and grey areas in tax legislation

As per the survey results, a lack of clarity and grey areas in the activity of tax authorities for the survey respondents mostly vary between three areas. The most frequently mentioned are the following:

- International taxation and use of double tax treaties,
- Free of charge delivery of goods / provision of service,
- VAT refund tax administration.

Smaller number of respondents mentioned beneficial ownership and tax on sales right and refund for utilities during construction of the facility.



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Conclusions

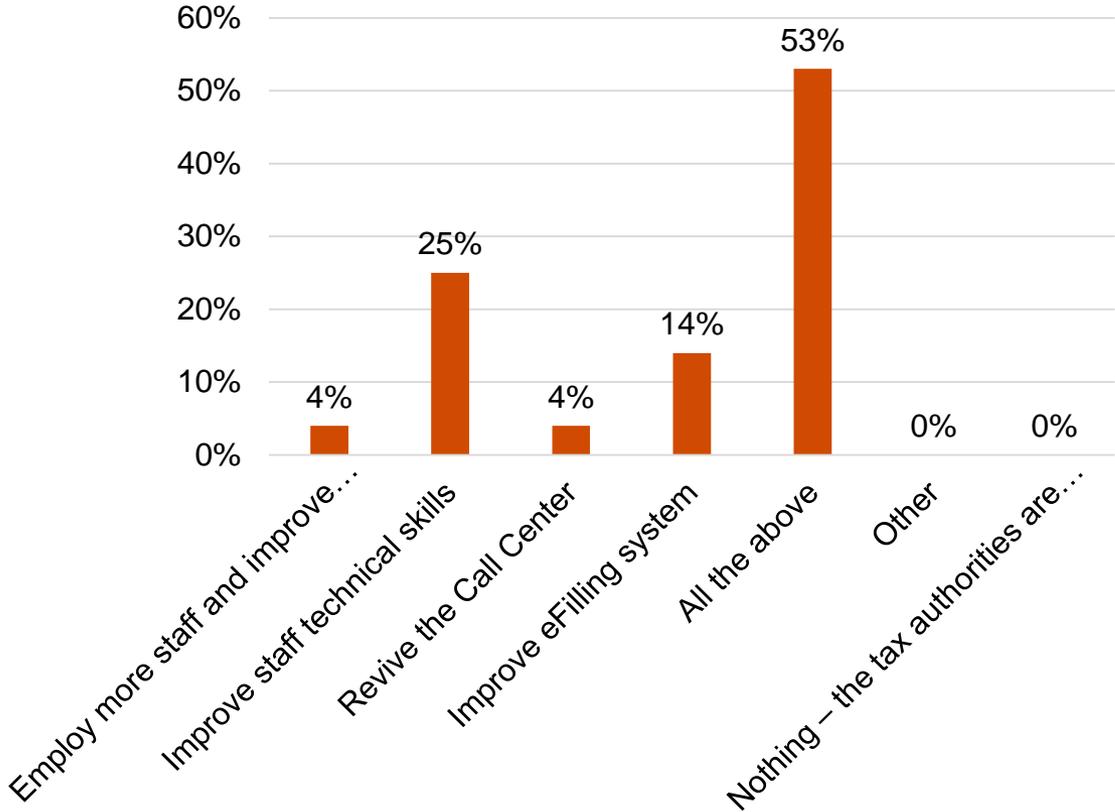
and

recommendations

Tax authorities improving its service offering to taxpayers

53%

As per the survey results, the majority of the respondents (53%) says that tax authorities should implement a series of measures to improve its service offering to taxpayers: employ more staff and improve turnaround time, improve staff technical skills, revive the Call Centre, improve eFiling system.



Conclusions

Duration and date of last inspection

- (62%) respondents noted that company's activities were affected as a result of tax inspections.
- An increase is noticeable in the number of tax inspections conducted in 2018 (64% of the respondents).

Additional amounts assessed following tax inspections

- In (41%) of the cases, additional liabilities assessed by tax inspectors were lower than BAM 50,000.
- There were cases where the additional amounts assessed ranged between BAM 50,000 and 100,000 (13%), BAM 100,000 and 500,000 (17%).

Main aspects identified during tax inspections

- Under corporate income tax, the most common aspects pertained to the intra-group transactions (12%).
- The entitlement to input VAT deduction was indicated as being the most frequently targeted aspect (7%).
- Targeted topics under WHT section were the reclassification of non-resident's income (5%).

Appeals against tax assessment documents

- More than half of our respondents, 54%, chose not to appeal against the tax assessment documents issued following tax inspections.
- The main reason for the high number of businesses deciding not to challenge tax assessment documents could be the tax inspection findings have been accepted (77%) answers.

Lack of clarity and grey areas in tax legislation

The most frequent lack of clarity and gray areas mentioned are the following:

- International taxation and use of double tax treaties,
- Free of charge delivery of goods / provision of service,
- VAT refund tax administration.

Recommendations

What should you consider?

- Risk degree – the longer the period during which your business was not subject to tax inspections (five to ten years), the higher the risk of being targeted for tax scrutiny in the future. Ideally, you should conduct a mock inspection ahead of the actual one, to detect the risk areas you can deal with beforehand and remove the risk of incurring late-payment interest and penalties.
- Furthermore, it is advisable for you to conduct a specialty analysis to assess your company's standing in terms of risk criteria and to identify the remedial action for the potential flaws in order to be classed in a lower risk class.

How can we prepare ourselves?

- In order to challenge the tax assessment documents successfully, you should pay particular attention to your contracts with service providers.
- Also, you need to have documents that support the economic substance of the services, clear and matching documentary evidence (contracts, correspondence, job descriptions, internal procedures), for intra-group services, having supporting documents showing the costs allocated to Bosnian-based affiliated undertakings and the allocation key used.

How can we defend ourselves?

- Preparing for tax inspection – it is advisable for you to consult tax and legal professionals to benefit from practical experience throughout the process, to prepare for inspection and to review the contracts and the related supporting documents, and to secure assistance for the duration of tax inspections.
- Assistance for the duration of inspections and in court – it is advisable for you to consult professionals to provide relevant assistance for the duration of a tax inspection and, especially, in court, where support is definitely needed.



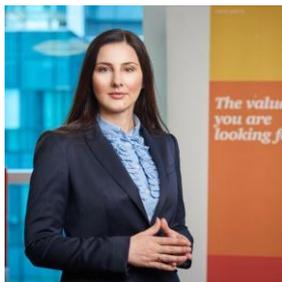
The conclusions in this presentation take into account the average of the results obtained only from this survey, as well as data from public sources or from public authorities, which we have not independently verified.

The recommendations in this material are of a general nature and based on our relevant experience and the statistics obtained. However, we stress that our above recommendations should not be regarded as universal remedies or applicable by default, because the specifics of each situation need to be considered.

Our main recommendation is for you to assess tax issues or aspects on a case-by-case basis, based on a specific analysis taking all relevant elements into account as accurately as possible and provide the best solutions or proposals to the specific situation. We are available to carry out these specific analyses together with you.

We are also available, on request, to conduct surveys on other topics of interest to you, focusing on agreed criteria (industry, topics, etc.), to the extent that the proposed topics are relevant and topical in the taxation field.

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Thank you

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