

RECENT TRENDS IN THE REGIME OF TRANSFER TAX IN THE CZECH REPUBLIC AND SELECTED EU MEMBER STATES

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***Abstract:** The taxation of the transfer of immovable assets is a typical feature of tax systems of the majority of EU member states. However, each of them uses its rather large power to select its own approach and to project it into the national (intrastate) law. The massive re-codification of the Czech Private law offered an opportunity to re-evaluate and to change the setting of the famous Czech tax triad, included for over two decades in the Act No. 537/1992 Coll., on the inheritance, gift and real estate transfer tax. Taking effect as of 1st January 2014, this Act was cancelled and its agenda was split, specifically the provisions about the tax on the transfer of real estate were incorporated in the brand new statute, namely the legal measure of the Senate No. 340/2013 Coll., on the real estate acquisition tax. These dramatic changes in the Czech transfer tax scenery need to be described and critically analyzed while using an assessed domestic questionnaire search and providing comparative comments regarding other EU member states.*

***Keywords:** Tax, Transfer, Tax return, Real estate, Guidelines value, Comparative value, Expert appraisal.*

***JEL Classification:** C18, H21, K34, R31, R38.*

Introduction

Most developed countries tax the change of the ownership of real estate, and thus the inheritance tax, gift tax and transfer tax regarding real estate are included in the majority of national tax systems [4]. Although the yield from the transfer tax is only 1% of the total state budget revenues in OECD countries, it is considered critical and is the subject of an intense debate involving economic, legal, and social arguments [4].

The taxation of immovable assets transfers is a typical feature of tax systems of the majority of EU member states. Nevertheless, there are significant differences in the perception of their foundation and function, and since the European integration is rather less pronounced in this arena, it basically devolves upon each and every member state to select its own approach to the transfer taxation and how it projects into the national (intrastate) law. Since the current (or just freshly passed) crisis has had a definitely punishing impact on the EU, the EU concepts, fundamentals and goals are undergoing a serious scrutiny influenced by practical and pragmatic considerations [7]. Thus, unlike regarding special ad hoc projects, a much more intense and stronger integration in national tax fields of EU member states in general does not seem to be at the top of the list of desired near future events [5]. In addition, there is an ongoing debate and many involved aspects are sensitive because they touch a number of social priorities which are not easy to be reconciled. This inherent dynamic makes this field prone to national legislation changes.

On 1st January, 2014, there took effect the Act No 89/2012 Coll., the New Civil Code (“New Civil Code”) which was created within a framework of a robust re-codification of the Czech national Private law. This re-codification of the Private law has an impact in the

arena of the Public law and consequently the former system of the Czech triad tax based on the Act No. 537/1992 Coll., on the inheritance, gift and real estate tax was changed and the agenda was split. Newly, the modified regulation of the inheritance and gift tax is added into the Act No. 586/1992 Coll., on the income tax, and the regulation of the former real estate transfer tax is included in the new legal measure of the Senate No. 340/2013 Coll., on the real estate acquisition tax (“Legal measure”). The new regulation of the real estate acquisition modifies the regime of the setting of the tax duty, allows the selection of the taxpayer of the real estate acquisition tax and brings new forms and templates. Thus, it is highly instructive to analyze and evaluate this new scenery from various perspectives and comparatively confront it with the *status quo* in several other EU member states and consider related legal as well as economic aspects.

1 Goals and methods

The first goal of this article is an analytic description and critical evaluation of the new regime of the real estate acquisition tax in the Czech Republic, based on the Legal measure and its comparison with matching regulations in selected EU member states. The second goal is the evaluation of the awareness about it, based on a questionnaire search assessed by the analysis of categorical data, i.e. whether individuals are sufficiently informed about the legal changes in the field of the real estate acquisition tax and, more specifically, whether the newly regulated possibility of an agreement between the seller and buyer about the determination of who pays the real estate acquisition tax will have any influence on the price of the real estate. The poll of questionnaire respondents consists of individuals currently selling or buying real estate in Prague and the questionnaire covers both, the issue of the level of the awareness and the issue of the possible influence of the possibility to determine the taxpayer on the sale price.

Therefore the hypotheses are set as follows:

- H1 – individuals are not sufficiently informed about changes in the field of the real estate acquisition tax;
- H2 – the newly regulated possibility to determine the taxpayer by the agreement of the seller and buyer will have an influence on the price.

At the outset, there was employed the method of the literate research including former and new legislation and then followed an evaluation by the comparison techniques. The analytical assessment of the cadastre of real estate and its data had deductive features and was closely linked to the prior literate research and its results. Hypotheses were set based on the professional search and its assessment while employing the categorical data analysis. The data extracted from the completed questionnaires was assessed by a categorical data analysis with the employment of the software program STATISTIKA and there was employed the statistic method of the dependency quantitative signs of Pearson’s chi-quadrante. The quantitative methods and meta-analysis could not be fully employed due to the extent of the research, but at least the discrepancy of the primary knowledge of respondents, while addressing the second hypothesis was reduced by an appropriate instruction provided before answering the second part of the questionnaire.

2 Real estate acquisition tax

2.1 Characteristic features of the real estate acquisition tax and of the Legal measure

European integration represents a concept perceived as a complex unification procedure entailing an abundance of complicated processes in various fields [9] and with a variable level of conferral competencies. The real estate transfer tax field is, and probably will stay in the near future, in the sphere of national competencies, i.e. out of a massive EU unification stream. Thus, the real estate transfer is taxed according to national laws of EU member states which are partially similar and this is more a result of the recognition of a similar value and tradition, practicability and global economy than due to Brussel's legislation.

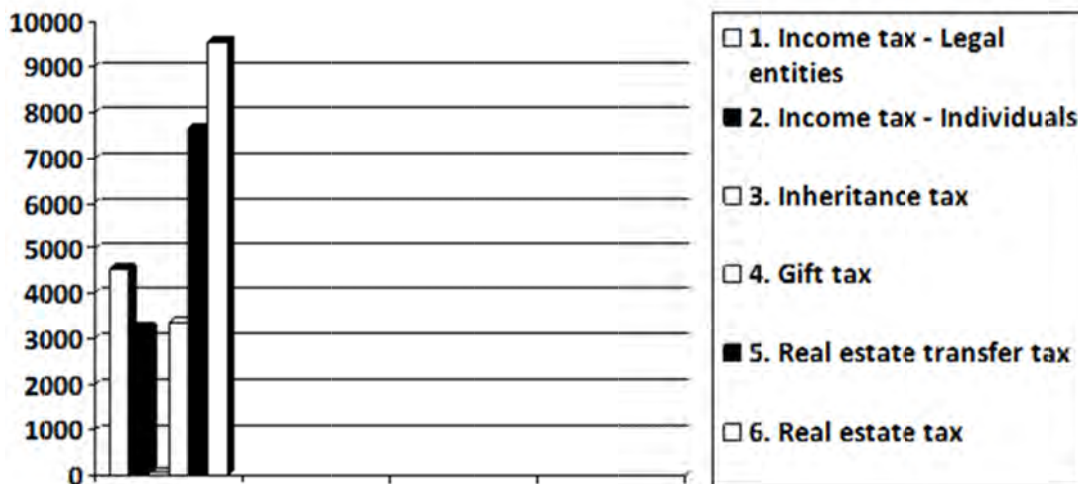
On 1st January, 2014, there took effect the New Civil Code, which emerged within the massive project of the re-codification of the national Private law of the Czech Republic. Hence, a large section of the Private law sphere is newly regulated by the New Civil Code and this gives a much stronger, noticeable and widely applicable importance to the contractual freedom and the concept of good morals, which are becoming automatically an integral part of the public order mandate [6].

Along with it took effect, as well, the Legal measure regarding the tax duty to be paid in the event of the transfer of the ownership of real estate which is neither through inheritance or gift. Real estate as the underlying object is newly defined by the New Civil Code in Art. 498 al.1 as land, under-terrain buildings with an independent purpose designation as well as real rights, i.e. *in rem* rights, to them, and rights designated to be real estate by the law. If the law states that an item is not a part of a piece of land and if such an item cannot be transferred from one place to another, then even this item is considered real estate. Hence the former definition of real estate by Act No. 40/1964 Coll., Civil Code including only houses, buildings, flats and land was newly expanded. Furthermore, newly the taxation will extend to the acquisition of real estate by possession during the prescription period and by expropriation. On the other hand, the Legal measure does not cover the real estate acquisition by land adjustments and by providing a compensation for expropriation.

The reason for the enactment of the Legal measure was the need to assure the continuity of the legal regulation of real estate transfer taxation, since the Act No. 357/1992 Coll, on inheritance, gift and transfer tax was cancelled.

The real estate acquisition tax is, as other taxes, the income of the state budget. The satisfaction of this duty is controlled by the relevant financial administration, according to the location of the real estate.

Fig. 1: Overview of various type of tax income into the state budget in 2012 in millions of CZK

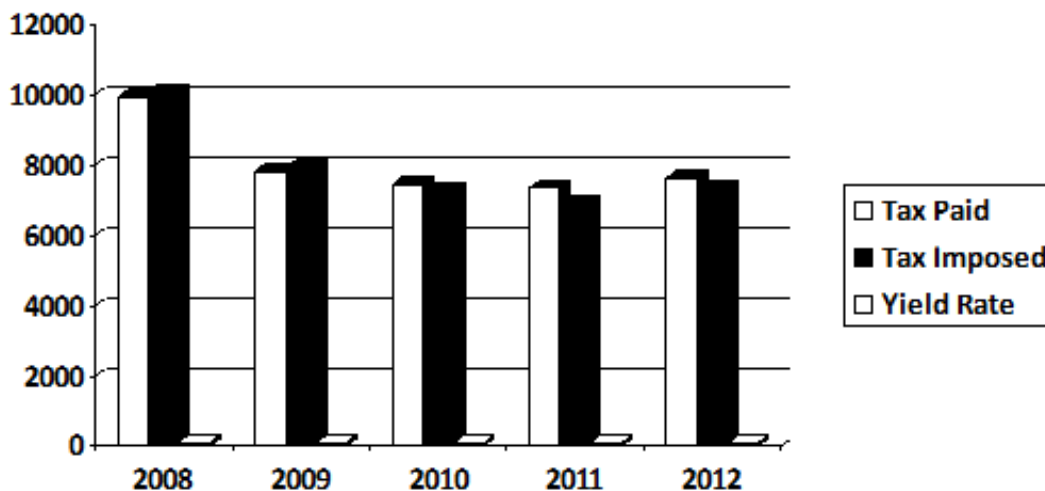


Authors Note: values are sorted from left to right

Source: [3]

In 2012, the biggest income in the state budget was generated by the real estate tax, totaling 9.541 million of CZK, followed by the real estate transfer tax of 7.660 million of CZK and by the income tax of legal entities in the amount of 4.538 million of CZK. The smallest contribution to the state budget came from the gift tax in the amount of 3.368 million of CZK and the income tax of individuals in the amount of 3.261 million of CZK [3]. Fig. 1 demonstrates the potential for the importance of the real estate acquisition tax for the income part of the state budget.

Fig. 2: The evolution of the payment of the real estate transfer tax in 2008 – 2012 in millions of CZK



Source: [3]

Fig. 2 shows the drop in 2009 due to the economic crisis, and it indicates the following stabilization at a rather lower level due to the general decrease of the price of real estate, as well as the volume of transactions. Furthermore, it demonstrates a moderate increase of 4% of the transfer tax in 2012, i.e. by 298 million of CZK and reached 7.660 million of CZK [3]. It suggests a partial revival of activities on the real estate market, perhaps even the winding-down of the world economic crisis.

2.2 The payer of the real estate acquisition tax

According to the former, as well as new, regulation, the payer of the real estate acquisition tax is the seller and the guarantor for the tax payment is the buyer, but the new regulation offers an option to the buyer and seller to agree that the buyer is the taxpayer and thus the guarantee-ship for the tax payment is eliminated [2]. This option should increase the certainty of the buyer that the tax duty will be timely and duly satisfied. However, the impact of this option and of its use on the amount of the sale price of the real estate is so far unclear.

The time limit to file the tax return regarding the real estate acquisition tax remains the same in the Legal measure as it was under the former legislation, i.e. the tax return needs to be filed on or before the last day of the third month following the month during which the cadastre registered the title change. For the real estate not registered by the cadastre or another public registry, the three month period starts to run from the date of the signature by the last party.

The locally competent tax administration is the tax administrator from the place of the pertinent real estate and in the above deadline applies for both, filing the tax return and paying the tax (down-payment on the tax). If the real estate acquisition tax does not exceed CZK 200, the tax is not to be paid.

2.3 Tax basis and rate for the determination of the tax duty

A real estate transfer tax is calculated as a rate applied on the tax basis. The Czech tax rate for the real estate acquisition tax is 4% of the tax basis. Interestingly, there is a large difference between developed countries in the amount of the transfer tax rate. Even more interestingly, the differences are matching on the both sides of Atlantic, i.e. 20% of the states in the USA and 20% of the EU member states have this rate as 0 or close to 0 and thus the real estate tax is not collected or collected in a symbolic amount. The remaining 80% of states charge at a rate 1-5% for the USA and at a rate 1-15% in the EU member states. Namely, certain regions in the EU which are considered as “wealthy” and with a strong drive for social re-distribution do not hesitate to set the rate way over 10%, e.g. regions in francophone countries or rich German towns such as Berlin or Hamburg [1]. It is worthy to observe that the rate is not flat in all EU member states and e.g. in the UK a strong tax rate progression applies with respect to real estate transfer tax rate going from 0% to 15%.

All EU member states struggle to some extent to the establishment of the tax basis to which the real estate transfer tax rate is to be applied. More generally, the valuation of real estate is a central tenet for all businesses, since land and property are factors of production [8] and at the same time have a strong social impact. There is a wide range of purposes for which valuations are required, including the real estate transfer tax, and many traditional (regression models or comparable, cost, income, profit method, etc.) as well as advanced (ANNs, hedonic pricing method, special analysis methods, ARIMA models, etc.) valuation methods can be used [8].

In the Czech Republic, the basis for the calculation of the real estate transfer tax is the so called acquisition value of the real estate reduced by the in the tax returned indicated recognized expenses, typically the costs of the expert appraisal. The acquisition value of the real estate is the agreed price, comparative tax value, the price according to an expert appraisal or a special price of the real estate. Hence, the Legal measure offers four methods

for the determination of the acquisition value of the real estate for the purpose of the real estate acquisition tax.

The first is the agreed price, and it is understood as the agreed and paid price. The second is the comparative value and it amounts to 75% of the guidelines value or the price according to an expert appraisal, and, if both are available, then the choice between these two belongs to the taxpayer. The guidelines value is calculated by the tax administration itself, based on data provided by the taxpayer about the real estate, such as the size, type, age, etc. and included in the tax return as a price of such real estate in the pertinent location. The calculation of the guidelines value does not require any expert appraisal and pursuant to the Explanatory Report to the Legal measure [2] this should reduce the administrative burden. Hence, the taxpayer pays only a down-payment in the amount of 4% from the acquisition value and after the calculation of the final tax duty by the tax office, this down-payment is transformed in the payment of the tax and if the calculation of the tax administration leads to a higher amount of the guidelines value, i.e. comparative value, the taxpayer thereafter must pay the difference. The third is the price according to an expert appraisal, and it is further regulated by the Act No. 151/1997 Coll., on the propriety assessment and its regulation. The fourth is the special price as a real estate acquisition price as set in the auction within bankruptcy or execution proceedings.

3 General information on the questionnaire search

Based on the questionnaire search and its assessment by the categorical data analysis, there was examined whether individuals are sufficiently informed about the changes in the field of the real estate acquisition tax and whether the newly regulated possibility to determine the taxpayer by the agreement of the seller and buyer will have any influence on the price. The questionnaires were presented to a pre-selected category of respondents, namely individuals selling or buying real estate in Prague. Two important and well-known real estate companies assisted in the process.

A two-phase filling of questionnaires was applied, i.e. the respondents answered the first part about their awareness, then they obtained information about the changes and thus the inequality of their original knowledge level was minimized and thereafter completed the second part about the possible impact of the contractual option to identify the taxpayer on the price.

In total, 50 questionnaires were distributed and all were correctly completed and returned. The obtained information, and extracted data, was assessed by categorical data analysis with the employment of the software program STATISTIKA. The importance level was set as $\alpha=0,05$ and the assessment itself occurred based on the statistic method of the dependency quantitative signs of Pearson's chi-square. The conditions for the use of the chi-square were met ($n>40$).

3.1 Results of the questionnaire search

H₁ – individuals are not sufficiently informed about changes in the field of the real estate acquisition tax

H₀ – there is no dependency between the indicated signs, i.e. individuals are sufficiently informed about the changes in the field of the real estate acquisition tax.

Tab. 1: Contingency table for H1

	Sufficiently informed	Insufficiently informed	Total
Buyers	8	17	25
Sellers	16	9	25
Total	24	26	50

Source: Authors

The value of the Pearson's chi-square is $X^2 = 5,12$. The importance level is $\alpha=0,05$ thus $X^2_{0,05 (1)} = 3,841$. Since $X^2 > X^2_{0,05 (1)}$, H_0 is rejected. This means that there is a dependency between the indicated signs, i.e. individuals are not sufficiently informed about the changes in the field of the real estate acquisition tax.

H2 – newly regulated possibility to determine the taxpayer by the agreement of the seller and buyer will have an influence on the price.

H₀ – there is no dependency between the indicated signs, i.e. the newly regulated possibility to determine the taxpayer by the agreement of the seller and buyer will not have an influence on the price of the sold real estate.

Tab. 2: Contingency table for H2

	Influence on the value of the real estate	No influence	Total
Buyers	6	19	25
Sellers	11	14	25
Total	17	33	50

Source: Authors

The value of the Pearson's chi-square is $X^2 = 2,22$. The importance level is $\alpha=0,05$ tzn. $X^2_{0,05 (1)} = 3,841$. Since $X^2 < X^2_{0,05 (1)}$, H_0 is confirmed, i.e. there is no dependence between the indicated signs and thus the newly regulated possibility to contractually determine the taxpayer will not have any impact on the sales price.

4 Discussion regarding the results of the questionnaire search

According to the questionnaire search and its assessment by the method of dependency of quantitative signs of Pearson's chi-square, individuals are not sufficiently informed about changes in the field of the real estate acquisition tax and the newly regulated possibility to determine the taxpayer by the agreement of the seller and buyer will have not an influence on the price of the sold real estate. In other words, respondents suffered by a lack of information, nevertheless even after having being informed they still stated that the contractual freedom to determine the taxpayer would not have any impact on the amount of the negotiated price. These quantitatively measured self-statements do not reflect qualitative aspects and should be reassessed in the future. It will be instructive to see if the parties, despite proclaiming the insignificance, will at least intuitively reflect the positive effect of the contractual possibility to determine the taxpayer, i.e. to make sure that it will be

the buyer. The result may be either that the new possibility will not be employed and remain without an impact on the price, or that the new possibility will be employed. In such case, either again it may either not dramatically impact the structure of real estate deals or it may increase the security of the transaction and decrease their complexity and ultimately generate a moderate change in real estate prices.

Conclusion

The intent of the legislature was to facilitate real estate transactions and to provide a more suitable and modern legal framework based on the recognition of the freedom of parties to determine how they will satisfy their public law duties, namely the determination of control of the tax basis and the payment of the real estate acquisition tax. The questionnaire search suggested that individuals are not sufficiently informed about these changes, and even after they became informed, they designated them as insignificant. These outcomes clearly demonstrate a deficiency in the informative and awareness campaign. Further, they indicate a rather questionable refusal of the fact that the legislative changes have a strong potential to simplify real estate transactions, to reduce the transaction costs by eliminating the expert appraisal costs, or to avoid payment for security deposits with respect to the part of the real estate price “frozen” for the payment of the tax duty.

A mere observation of the future praxis along with further research including qualitative aspects and the employment of meta-analysis methods should bring more light in this, so far, rather unclear and confused arena, and help with the final answer whether the intent of the legislature becomes materialized.

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