

TaxAlert

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In its session of Friday, 24 July 2009, with the aim of introducing anti-recession measures, the Croatian Government proposed a new Law on special tax on salary, pensions and other income which would be applicable until 31 December 2010.

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Law on special tax on salaries, pensions and other income

We set out below an overview of the main provisions of the proposed Law on special tax on salaries, pensions and other income, as well as of the difficulties which might be faced in practice in applying this Law. The introduction of this special tax should generate income in the amount of HRK 2.12 billion.

The special tax on salaries, pensions and other income is payable on salaries, pensions and other income paid on or after the date when the Law becomes effective *until 31 December 2010*. As the Law becomes effective on the date of issuance in the Official Gazette, if it is adopted, it is still uncertain whether it would apply as of 1 August 2009 or as of a later date.

Taxable base

As the name itself says, the following are subject to the new special tax:

- Employment income
- Pensions
- Other income¹

The taxable base is net income, that is, salary, pension or other income *after* deduction of compulsory social security contributions, tax deductible insurance premiums (e.g. life insurance premiums, voluntary pension insurance), personal income tax and city surtax withheld, but *before* any deductions from net income (e.g. deduction of loan annuities).

Tax rate

| Net income ² (HRK) | Special tax rate |
|-------------------------------|------------------------|
| 3,000 – 6,000 per month | 2% on total net income |
| Above 6,000 per month | 4% on total net income |

Obligation to assess and pay special tax

The person obliged to assess, withhold and pay the special tax on salaries, pensions and other income is the payer of

salary, pension or other income.

Payment of special tax and calculation period

The special tax on salaries, pensions and other income needs to be paid at source simultaneously with the salary, pensions or other income to a designated account (which should be made available within 30 days after the Law comes into effect).

Reporting

Payers of salaries, pensions and other income are required to submit a prescribed form (which should also be made available within 30 days from effectiveness of the Law) to the Tax Authorities until the 15th of the month, for the previous month.

Under the assumption that the new Law on special tax on salaries, pensions and other income would become effective as of 1 August 2009 and, since it would apply to income *paid out* as of that date, this would mean that the first set of forms would need to be filed by 15 September 2009 (for the month of August) and the Minister of Finance should prescribe the format of these forms by the end of August.

Implementation acts

The Minister of Finance is required to issue the regulations on implementation

¹ As defined in Article 32 and 33 of the Personal Income Tax Law, including receipts by management board members, sportsmen, freelancers, authors royalties, etc.

² Income relating to prior periods received based on court rulings is not subject to special tax on salaries, pensions and other income, regardless of the amount.

of the Law on special tax on salaries, pensions and other income, as well as on the content and format of the above mentioned forms, within 30 days after the Law on special tax on salaries, pensions and other income becomes effective.

Possible difficulties in application

As the special tax is payable on net income, that is, after deduction of, amongst other, tax deductible insurance premiums, it is likely that the application of the above mentioned provisions could cause difficulties in cases where the payer of salary, pension or other income does not pay tax deductible premiums on behalf of the recipient of income, but the recipient of the income pays these premiums by himself/herself.

As a result, the payer might withhold special tax even though, if the tax deductible insurance premiums paid by the recipient of income were taken into consideration, net income would not exceed the above mentioned thresholds, that is, a lower rate of special tax should have been applied. The currently proposed Law does not provide for the possibility to submit an annual personal income tax return in such cases, which would enable the recipient to correct the calculation, that is, to obtain a refund of overpaid tax.

Further, another issue that could arise is in cases where individuals have several sources of income, that is,

where an individual receives employment income, as well as other income.

As the special tax is payable on the amount of total income received during one month, the payer of a particular type of income would need to be aware of how much the respective individual might have already earned in that month in order to be able to determine whether any special tax should be assessed at all (in case total income of the individual amounts to less than HRK 3,000) or at which rate the special tax should be assessed.

Penalties

| Offence | Late payment of special tax | Late submission of forms |
|------------|-----------------------------|--------------------------|
| Company | HRK 20,000 – 500,000 | HRK 20,000 – 500,000 |
| Individual | HRK 5,000 – 100,000 | HRK 5,000 – 100,000 |

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The full Croatian version of the draft Law can be found on this [link](#).

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