



Our latest newsletter brings you lots of tax news. Enjoy the reading. We enjoy this year's spring. We do not mind the never ending winter since we spend most of the day in the office.

Currently, we are engaged in many interesting projects. One of them is tax transactional advice related to an **acquisition of a hotel** located in the Prague centre, the value of the transaction was EUR 20 million. Another is related to acquisition of **a shopping centre**, the value of the transaction was EUR 10 million.

We were approached by a new client, a producer in heavy industry whose turnover is a few billion of Czech crowns.

We have been listed in the prestigious worldwide directory Legal 500 years ago, this year we were moved to 2 tier among other respectable legal firms. Thank you for your support and we are looking forward to working with you again.

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### **Amendment to tax laws finally approved**

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### **Prepared changes to international measures against tax evasion**

On the basis of international activities of the Organisation for Economic Cooperation and Development (the OECD) against base erosion and profit shifting (the BEPS programme), two EU directives were approved last year.

### **Information published by the General Financial Directorate in 2017**

The Financial Directorate published on their web pages information on extension of the possibility to waive a penalty related to not submitting an inspection report, the reverse charge for electronic communication services, and the electronic record-keeping of cash sales.



## Amendment to tax laws finally approved

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On this day, most of the changes to value added tax and some changes to income tax will become effective, and these will be relevant to the 2017 tax period. These include, for example, an increase in tax advantages for second and third children or changes to the application of lump-sum expense allowances. Part of the changes to income tax will become effective from the 2018 tax period, or their effectivity will depend on the moment the long-term assets are classified or their depreciation commences, or on the moment the subject matter of financial leasing is handed over.

We informed you about the amendment in our KempHoogstad Tax News published at the end of the previous year. We describe below only the selected changes we had not informed you about before since we had already expected those to change:

- (i) *Reduction of the maximum amounts of lump-sum expense allowances for self-employed persons or persons with income from renting real estate and cancellation of the limitation of tax reliefs to tax*

The maximum amounts of lump-sum expense allowances that can be used by self-employed persons or persons with income from renting real estate will be reduced by half. The percentage for calculation of the expense allowance will remain unchanged. A tax payer whose income is CZK 1,000,000 will reach the maximum lump-sum expense allowance, and the lump-sum expense allowance stays constant for any higher income. On the other hand, tax payers using lump-sum expense allowances can claim again tax reliefs for a spouse and tax advantages for children with no limitations.

Tax payers with income above CZK 1,000,000 can make a choice regarding the accounting year 2017: they can use the lump-sum expense allowances in the reduced maximum amount and at the same time claim the tax relief and advantages, or they can use the lump-sum expense allowances in the current amount and their claim for tax relief and advantages will be limited. Tax payers with income of less than CZK 1,000,000 can claim the tax relief for a spouse and the tax advantages already in the 2017 tax period since their maximum amount of expense allowance does not exceed the new limit.

- (ii) *Additional possibilities for self-employed persons to apply for calculating income tax with a lump sum*

Self-employed persons who have employees or income from dependent activities can now apply for calculating income tax with a lump sum.

- (iii) *Binding assessment of the method for stipulating the tax base of a permanent establishment*

Tax non-residents can request a binding assessment regarding whether the method used for stipulating the tax base or the tax loss from activities provided through a permanent establishment results in a lower tax base



or a higher tax loss compared to the tax base or tax loss resulted from the same or similar activities performed under similar conditions by a Czech tax resident.

(iv) *Changes related to the VAT liability upon the date of receiving of payment*

The obligation to pay VAT from a received payment or to report the exempt supply when receiving a payment will be now used when the supply (of goods or services), the tax rate, and the place of supply are sufficiently known as at the day of receiving the payment. This change can noticeably influence the VAT treatment of provision of various vouchers or prepaid services.

Finally, we would like to inform you that the 2017 tax period introduces higher limits for deduction of pension and life insurance for the taxation of individuals; the current maximum amount of CZK 12,000 per year increases to CZK 24,000 per year. Moreover, the limit for tax exempt contributions to pension and life insurance paid by employers to their employees increases from the current total amount of CZK 30,000 to CZK 50,000 per year.

## Prepared changes to international measures against tax evasion

On the basis of international activities of the Organisation for Economic Cooperation and Development (the OECD) against base erosion and profit shifting (the BEPS programme), two EU directives were approved last year. These are the directive regarding mandatory automatic exchange of information and the Anti Tax Avoidance Directive (the ATAD). Preparations for implementing the two directives into Czech legislation are under way.

(i) *Automatic Exchange of Information*

The Directive introduces the obligation for international groups whose consolidated turnover for the previous accounting period exceed EUR 750 million to submit the Country by Country Report. The Report will be prepared by the group via a chosen entity which will submit the Report to a tax administrator who, under the Automatic Exchange of Information Directive, will provide the Report to all the countries where the group has its activities. The Report will contain overall information on the international group and on the individual entities within the group, so cooperation of the remaining entities for the purposes of completing the Report will be required. The respective governmental proposal of the act introducing the obligation into Czech legislation is now being debated in the Chamber of Deputies. The act should be effective – with respect to the Directive – on 5 June 2017 at the latest.

With respect to the Automatic Exchange of Information Directive, an amendment to the International Cooperation in Tax Administration Act was approved. The Act, with effectiveness from 1 April 2017, introduces the automatic exchange of information on preliminary tax decisions and preliminary assessments of transfer prices which were issued by the tax administration of one state but which have an impact in another tax



jurisdiction. From the Czech point of view, the exchange of information concerns decisions on the binding assessment of the method used for the calculation of prices between related persons.

(ii) *Rules against tax avoidance practices*

With respect to implementation of the rules into Czech legislation, the Ministry of Finance published detailed discussion papers that summarise the individual rules and outline the possible variations of their implementation. The papers include namely drafts of the rules stated below:

- The rule limiting the tax deductibility of excessive borrowing costs to 30 per cent of EBITDA. The costs should include interest and other costs related to debt and similar instruments (provided not only by related persons) in the amount by which they exceed the taxable interest revenue. Basically, the rule should be used on all entities with a potential exemption of financial businesses and entities outside the group. There is a proposal not to apply the rule if the excessive borrowing costs do not exceed EUR 1 million.
- The rule introducing exit taxation, which means that tax should be imposed on the difference between the market and tax value of assets which will be transferred by the tax payer to another state, for example, when the assets are transferred in or from a permanent establishment, when the tax residency is transferred, or when the business activities are transferred. The effectiveness of the rule can be postponed until 1 January 2020.
- The rule for taxation of incomes of a controlled international entity under the tax base of the parent company residing in the Czech Republic (the CFC rule) which should prevent profit shifting to subsidiaries in countries with a lower level of taxation. The proposal suggests that, for the purposes of the rule, the share in the controlled entity should be higher than 50 per cent, and the tax would be imposed if the level of taxation of the controlled entity abroad is less than one half of the tax paid in the Czech Republic. There should be defined certain exceptions when the rule would not be used.
- The rules regulating "hybrid discrepancies", i.e. situations when, due to different intrastate regulations of individual states (e.g. in the legal definitions of subjects, financial instruments, permanent establishment), tax advantages can be achieved, for example, in the form of double non-taxation of income or double reduction of the tax base via a deduction of the same costs. The rule should cover hybrid discrepancies within the member states and with respect to third countries.

The rule concerning tax deductibility of financial costs and the CFC rule should become effective from 1 January 2019. The Ministry is considering postponing the effectiveness of the exit taxation rule and the hybrid discrepancies rule until 1 January 2020.

Finally, we would like to inform you that, under the BEPS programme, the OECD approved the wording of a new multilateral treaty at the end of last year. The countries that will join the treaty will be obliged to respect measures against base erosion and profit shifting when applying individual double taxation treaties. The measures will concern misuse of the double taxation treaties, methods of solving disputes over double taxation, avoiding the status



of a permanent establishment, and neutralisation of the effects of the hybrid schemes. It is expected that the Czech Republic will join the multilateral treaty. The multilateral treaty governs the way the individual countries apply the measures to already concluded double taxation treaties.

## Information published by the General Financial Directorate in 2017

The Financial Directorate published on their web pages updated guidance note D-29 and other information on extension of the possibility to waive a penalty related to not submitting an inspection report. Further, there is updated information on applying the reverse charge regime for electronic communication services and new information on the interpretation of some provisions of the Electronic Record-keeping of Cash Sales Act was published.

### **Possibilities for waiving penalties related to inspection reports extended**

It is now possible to apply for completely waiving up to two penalties charged for errors that occurred in 2016 and one penalty for an error that occurred in 2017 without giving any specific reason. There is a condition that the tax payers have not seriously violated the tax or accounting regulations in the preceding three years.

It is currently also possible to apply for waiving a penalty when the payer has answered an appeal to submit an inspection report or to correct a discrepancy but the payer did so too late, though within five days at the latest of the official deadline, and at the same time, in a situation where the payer was not obliged to submit an inspection report or when the payer confirms the correctness of the originally submitted report.

The guidance note reflects a finding of the Supreme Court which revoked Section 101(g)(5) of the VAT Act, effective from 15 February 2017. According to this provision, the Financial Authority could consider an appeal for submitting an inspection report as delivered at the moment the tax administrator sends it via e-mail. If a penalty has been assessed in cases where the appeal was delivered via e-mail only from 1 January 2016 to 15 February 2017, there is a possibility to apply for completely waiving the penalty.

Before sending an application for waiving a penalty, we recommend carefully reading the above-mentioned instruction which describes the issue in detail. The application for waiving a penalty is subject to an administration fee of CZK 1,000.

### **Updated information on applying of the reverse charge regime for electronic communication services**

The reverse charge regime of VAT for electronic communications services provided among entities carrying out business on the wholesale level in the Czech Republic has been valid since 1 October 2016. The newly published additional information gives details on applying the regime for telecommunication services and, contrary to the original information released last year, says that the reverse charge regime will not be applied if the receiver buys the given



electronic communication service for its own needs or for the needs of other final users (e.g. employees, subsidiaries, tenants, guests in hotels, customers in restaurants).

### **Additional information on the Electronic Record-keeping of Cash Sales**

The General Financial Directorate published additional information on the moment of origin of the cash sale for payments made via the Internet. According to the information, tax payers can, under certain conditions, record the sale at the moment they learn that the payment was sent from the customer's account (i.e. not at the moment the payment order was assigned) or at the moment the goods are sent or the services are provided, if this precedes the moment they find out the payment has been made. The additional information is also about payments made via other payments systems.

The methodology was completed by issues concerning record-keeping of sales in cases where the cash payments are paid by customers to carriers who transport the goods; issues regarding assessment of minor activity for the purposes of a delay in the start of the ERCS with respect to the main activity (if the income from the minor activity is subject to the ERCS before the income from the main activity).

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