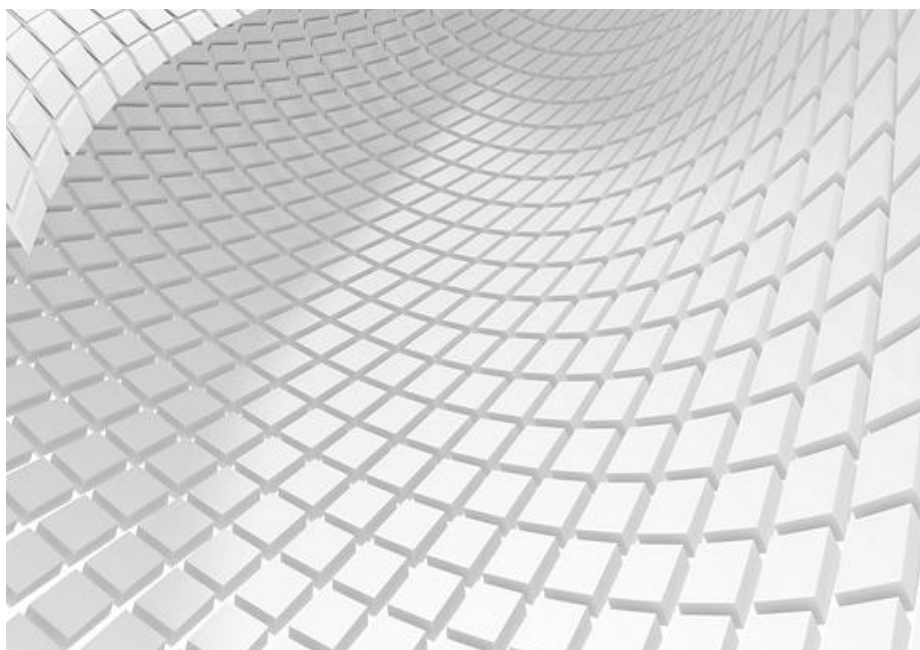


# KempHoogstad Tax News

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**KempHoogstad**

Tax Advice & Solutions

# 1. The Act on Proving the Origin of Property

The act, which introduces completely new provisions on proving the origin of property in the Income Tax Act, has been signed by the president.

The act, when already under preparation, was widely criticised by experts and consultants. It is considered a very strong instrument of the tax administration for verifying the legality of income. The approved provisions are very general, and their interpretation and use in real life will undoubtedly be problematic and questionable. Even though the Act will become effective soon (most likely from 1 November), there is no methodology available. The Act's provisions apply to persons and legal entities, and also to tax residents and non-residents. Regarding tax non-residents, the Act will not apply to income which tax payers are able to prove that they are not generated from sources in the Czech Republic.

We summarise below the basic parameters of the respective provisions.

## **Appeal to prove the origin and source of income**

The tax administrator is entitled to request from tax payers proof of the source and origin of income if

- || the tax administrator has a well-founded suspicion that the tax payer's reported income (especially in the tax returns or in notifications of exempt income) does not reflect the increase in property (i.e. increase in property with respect to debts), consumption, or other expenses<sup>1</sup>; and
- || the expected difference is more than CZK 5,000,000.

The decisive period for assessment of the tax payers' income and their property, consumption, or other expenses will be determined by the tax administrator. The tax administrator will determine the method of evaluation of individual parameters (i.e. evaluation of the property, consumption, or other expenses) that caused the mentioned doubts and issuing the appeal because the Act does not specify the evaluation issue. It is expected that the issue will be governed by a guidance note.

Tax payers will not be obliged to prove the facts in an appeal if they are able to prove that they happened in a period barred by the statute of limitations for the purposes of tax determination. This could be questionable in many instances, because the facts could have occurred in the past when a tax payer was not obliged to archive the respective documentation for any reason or legal obligation. The existing legal framework embodies especially the obligation of proving (i) facts stated in the tax returns and reports and (ii) facts needed for a correct tax stipulation. So far, the legislation has not contained the obligation to collect documentation related to the tax payers' consumption, or other expenses, or evidence of income used for acquiring the property.

Even if the tax payers prove that the facts required in an appeal happened in a time-barred period, there could be a situation where the tax administrator proposes a motion to law enforcement

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<sup>1</sup> Consumption or other expenses means, for example, the gratuitous use of property (a car, yacht, real estate, jewellery) or spending money that does not appear to be an increase in the payer's property.

authorities, because there is a suspicion a crime has been committed. If the tax payer is sentenced for a tax crime, the tax can be assessed even after the time-barred period.

The information that makes the tax administrator issue an appeal for an individual tax payer can be acquired by the tax administrators during their standard activities (i.e. searching and inspecting activities), or via cooperation with other public authorities, or because of initiatives from the public (e.g. denunciation).

### **Not proving the facts required by the appeal, tax assessment and penalties**

If a tax payer is not able to prove the facts requested in an appeal for proving income (e.g. there is a difference between the tax administrator's calculations which is caused by exempt incomes that are not subject to taxation) and the tax administrator concludes that (i) the tax cannot be assessed by proof and (ii) the tax assessed with the help of special instruments is higher than CZK 2,000,000, then the tax administrator assesses the tax with the help of special instruments.

Assessment of tax with the help of special instruments is newly embedded in the Income Tax Act. According to this assessment, the tax administrator can stipulated the tax base with the help of an estimate of the amount of the income which the tax payer had to have to acquire the respective increase in property, consumption, or other expenses. If the given income cannot be assigned to a tax period, the tax administrator will consider the incomes to have been generated in the last tax period for stipulating the tax.

So there can be situations where the tax payer, who correctly taxed its income in the past or who did not correctly tax its income (e.g. because of an exemption), will have to tax its income again, or wrongfully because the tax payer would not have at its disposal sufficient proof to comply with the tax administrator's appeal.

The tax payer will be obliged to pay the fine from the tax assessed with the help of special instruments, which will be either 50 per cent or 100 per cent of the assessed tax, if the tax payer does not cooperate sufficiently and seriously aggravates or thwarts the tax stipulation during the proceedings. The issue related to prohibiting self-recrimination is being discussed with respect to this.

If a tax payer does not prove the facts requested in an appeal but the tax can be stipulated by proof or the expected tax is not higher than CZK 2,000,000 and can be stipulated with the help of standard instruments defined in the Tax Code, then standard penalties from the Tax Code will apply.

### **Appeal to make a property declaration**

Under the Act, the tax administrator can request from a tax payer a property declaration which is specifically modified by the new provisions of the Income Tax Act. The tax administrator uses the appeal to make a property declaration if (i) the tax payer has not proved the facts requested by the appeal to prove the income, (ii) the information on the state of the payer's property cannot be obtained or obtaining it would be extremely difficult, and (iii) the supposed value of the property is higher than CZK 10,000,000.

If the tax payer does not submit the property declaration when appealed, or it presents untrue or seriously distorted data, the tax administrator will assess the tax with the help of special instruments with no other delay. If the tax payer does not submit the property declaration or presents untrue or seriously distorted data and hence commits a crime, it will face from six months to three years prison, disqualification, or a fine.

## 2. Guidance notes regarding the electronic registration of sales

The Tax Administration published a guidance note regarding implementation of the Act on the Registration of Sales on their web pages ([http://www.etrzby.cz/cs/novinky\\_metodika-k-evidenci-trzeb](http://www.etrzby.cz/cs/novinky_metodika-k-evidenci-trzeb)). The document is quite extensive, and it summarises all the information published on implementation of the act by the Tax Administration. The information is analysed in detail and is explained using examples. Moreover, it presents the interpretation of some terms that have not yet been explained. We select the most interesting information:

- || A tax payer should not be obliged to apply the electronic registration of sales if cash income is irregular. According to the guidance note, irregular income will always be determined by the specific circumstances, but basically such income should be one-time income or rare income. A regular payment should not be considered irregular income even if it does not occur often.
- || The Act excludes from the registration of sales the sales acquired from minor business activities of public-service oriented tax payers. According to the guidance note, a minor business activity will be considered such an activity that generated income/revenues for the tax payer in the previous calendar year that are less than CZK 175,000 or less than 5 per cent of the total income/revenues of the tax payer.
- || According to the guidance note, a tax payer should not be subject to the registration of sales because of its minor activity if the sales from the minor activity have been subject to registration in an earlier phase than the sales from the main activity. The minor activity is defined by the note as an activity that is not performed in separate business premises and payments from it make up a maximum of 49 per cent of all payments of the premises and are not higher than CZK 175,000 in the given premises. The payments are considered for the previous calendar year, and if there are more minor activities in one business premises, the total amount for the activities applies to the limit. This exception is not governed by the act but, according to the note, the exception is based on the basic principles of tax proceedings, i.e. the principle of efficiency and savings of others.
- || In the first phase, which starts on 1 December 2016, the registration of sales will apply to accommodation and catering services. The term "catering service" should be interpreted in basically the same way as the same concept defined for the purposes of VAT (i.e. a catering service should not be a "take away" sale when it involves the delivery of goods,

and the sale will be subject to registration of sales in the third phase, i.e. from 1 March 2018).

- || The registration of sales will apply also to payments via a payments system, such as PayPal, PayU, etc.
- || The note also deals with such issues – for example – when a payer returns a payment, tips, refundable deposits, payments made via CCS cards, payments received by more than one tax payer, charging and paying with prepaid cards, coupons, vouchers, etc.
- || According to the note, a receipt lottery should be launch in the first half of 2017.

Please note that, from 1 September, the tax payers can apply for authentication data that will be needed for logging into the tax administration web portal for the purpose of administration of their certificates and record-keeping of sales. The application for receiving the authentication data can be send via the tax administration web portal (the EPO application, using the data box log-in, or in person at any tax administration office). Only the two described ways can be used for applying, and a written application will not possible even if sent via a data box.

### 3. Amendment to the Real Estate Acquisition Tax Act

From 1 November 2016, the amendment to the Real Estate Acquisition Tax Act will be effective. We have informed you about its contents already.

The most important, and perhaps the most well-known, change is the one stating that the tax payer will now always be the acquirer of the real estate, which means that the sometimes troublesome principle of guaranteeing for payment of the tax will cease to exist. The decisive date for stipulating the tax payer with respect to the amendment will be the real date of acquisition of the property right, which is most frequently (i.e. when acquiring the property right to real estate recorded in the Real Estate Register) the day of the legal effect of the record in the Real Estate Register.

The subject matter of the tax will now be extension of building rights and acquisition of real estate via the transfer of assets to a partner. Transfers and transitions of real estate regarding other changes of business corporations as well as all legal entities will remain tax exemptions.

In the case of exemptions regarding the first paid acquisition of a newly constructed family house or flat unit in a residential building, the exemption will only be applied to finished or used buildings. The exemptions now do not apply to the acquisition of buildings or units under construction.

There is another interesting change: the subject matter of tax regarding the transfer of utility networks will only be the part of the utility network that is a building (e.g. a transformer station). Hence, the subject matter of the tax will not be, for example, the transfer of water or sewage pipelines or power lines.

Other changes include certain modifications related to determining the tax base in the case of interchange of real estate, extension of using guidance values, or specification of the recorded price in the case of acquisition of real estate as part of the acquisition of a business establishment. The Tax Administration published more information on the selected changes on their web pages

(<http://www.financnisprava.cz/cs/dane-a-pojistne/dane/dan-z-nabyti-nemovitych-veci/informace-stanoviska-sdeleni/informace-k-novele-zakonneho-opatreni-senatu-o-dani-z-nabyti-nemovitych-veci-7471>).

## 4. Changes to VAT

The amendment to the VAT Act prepared with respect to the amendment to the Customs Code became effective on 29 July 2016. We informed you about the amendment when it was being approved. The important changes are:

- || Changes to the application of VAT on imports and exports (especially cancellation of exceptions regarding free warehouses and free zones) with respect to changes to the Customs Code. A tax receipt for VAT purposes relating to the export of goods will now be a standard tax invoice, i.e. basically an invoice for goods.
- || Applying the reverse charge mechanism in the supply of goods with the place of supply based in the Czech Republic by a person not living in the Czech Republic to a tax payer. The amendment permits cancellation of the registration of respective payers during six months (persons not living in the Czech Republic) in the transitional provisions and under certain conditions. The working group at the Chamber of Tax Advisors already dealt with some unclear issues regarding possible de-registration.
- || Instead of the Financial Office for Prague, the Financial Office for the Moravia-Silesian Region will become the respective financial authority for tax payers who do not have a registered office or place of business in the Czech Republic. From 1 September 2016, new entities requesting registration will file their application at the mentioned Financial Office. The date the jurisdiction of the individual payer changes will be announced by the current local Financial Office. When changing the Financial Office, the bank account number where the tax payers will have to send their tax payments will also change.
- || Mitigation of penalties for the breach of duties related to the inspection report. New guideline no. D-29 deals in detail with the issue.
- || Adjustment of the provision for the correction of VAT in claims against debtors in insolvency proceedings confirming the original intent of the act to correct claims against debtors in insolvency proceedings for claims older than six months before the court's decision on bankruptcy

Following up on the changes regarding free warehouses and zones and applying the reverse charge mechanism in the supply of goods with the place of supply based in the Czech Republic by a person not living in the Czech Republic, the VAT return form and control statement have also changed. The new form can be used also for the tax period before the amendment became effective.

The government approved an extension of the reverse charge regime of VAT for selected telecommunications services provided among entities carrying out business in electronic communications (Act no. 127/2005 Coll., on electronic communications on the wholesale level), effective from 1 October 2016. The change does not affect services provided to final consumers.

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