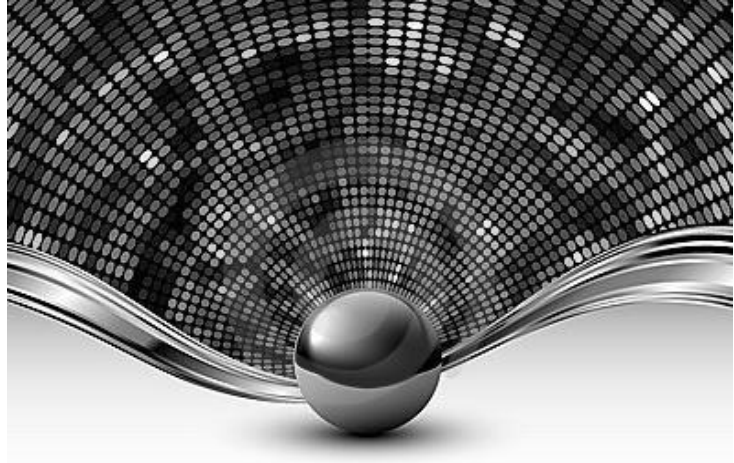


KempHoogstad Tax News

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Tax Advice & Solutions

1. Reverse charge mechanism in the supply of electricity, gas and supply of electricity certificates

Effective from 1 February 2016, the duty to apply the VAT reverse charge mechanism was also extended to some other performances. The mechanism will be newly applied to the below specified performances to the extent that the transaction is carried out within the territory of the country and the payer is the recipient of the supply:

- || supply of electricity certificates; and
- || supply of electricity and gas via systems or networks to a trader.

Trader means

- || a person who purchases gas or electricity primarily for the purpose of their resale and whose own consumption of these goods is negligible, or
- || a person whose subject of business involves electricity transfer, electricity distribution, trade of electricity, activities as market operator, gas transmission, gas distribution, gas storage and trade of gas under conditions laid down by law.

In principle, the status of the purchaser-trader is relevant for the application of the reverse charge mechanism. The purpose of the purchased commodity has no effect on the application of the reverse charge mechanism, i.e. the reverse charge is applied even when the trader purchases electricity or gas for its own consumption. According to information published by the Ministry of Finance (information at <http://www.financnisprava.cz/assets/cs/prilohy/d-seznam-dani/Informace-GFR-k-aplikaci-rezimu-prenesen-danove-povinnosti-u-dodani-elekriny-plynu-a-certifikatu-elekriny.pdf>), for the purpose of the reverse charge mechanism, trader means an entity licensed for the trade of electricity or trade of gas, notwithstanding the potential use of electricity or gas for its own consumption. Thus, the reverse charge mechanism is applicable even in a situation where an electricity purchaser is only licensed for trading gas and, vice-versa, where a gas purchaser is only licensed for trading electricity. Furthermore, entities engaged in trading only for the purpose of providing for the actual functioning of the electricity and gas market and whose activities are economically and technically related to the markets (e.g. electricity and gas transfer and distribution, activities as market operator, gas storage) shall be regarded as traders. However, a payer who supplies electricity or gas in connection with the lease of real estate is not considered a trader.

The above-mentioned information of the Ministry of Finance contains details on the supply of electricity certificates and general duties related to the reverse charge mechanism, e.g. for addressing a situation in which an advance payment for a transaction which is subject to the reverse charge mechanism was received before the reverse charge mechanism became applicable to that particular transaction, information on the determination of the taxable amount, including the application of the reverse charge mechanism on ancillary costs, as well as information on the specification of the relevant transactions in the follow-up report.

2. Electronic records of sales – development of the draft law

In early February the chamber of deputies passed a draft law on electronic records of sales, together with a draft accompanying law on a decrease in VAT for catering services, excluding alcoholic beverages, to 15%, and the introduction of an income tax allowance of up to CZK 5,000 for a payer whose duty to record sales arose in the relevant tax period under the Records of Sales Act.

The draft laws must still to go through the approval procedure in the senate and, subsequently, must be signed by the president. Assuming that the Records of Sales Act is promulgated in the collection of laws in June 2016, in the first stage the duty to record sales will begin to apply to providers of accommodation and catering services in November 2016. After three months, the duty to record sales will begin to apply to sales in the retail and wholesale sectors (stage 2) and, 15 months after launching, the duty will be extended to other activities (for example, transport, agriculture, liberal professions), with some exceptions (selected crafts and manufacturing activities), which will be subject to the duty to record their sales 18 months after stage 1 is launched.

After the completion of the approval process, we will inform you in detail about the final wording of the law and its contents.

3. Planned VAT changes

The government submitted to the chamber of deputies a draft new Customs Act which responds to the new EU Customs Code. Together with the draft, the chamber of deputies will discuss draft amendments to related laws, including some changes to the VAT Act. A brief summary of the most relevant amendments follows:

- i Change of territorial jurisdiction in relation to a taxable person without a seat or establishment in the national territory

Instead of the Tax Authority for the Capital City of Prague, the Tax Authority for the Moravian and Silesian Region will have territorial jurisdiction for such persons. The reason is an effort to free up capacity on the part of the Prague Tax Authority.

- ii Abolition of the special regime for free zones and warehouses

The placing of goods in a free zone and the delivery of goods in a free zone (including provision of related services) should be subject to VAT. The concept of free warehouses will cease to exist.

- iii The reverse charge mechanism in the delivery of goods as a transaction within the country by a person not established in the territory of the country to a payer

If a taxable person without a seat in the national territory delivers goods as a transaction within the country to a purchaser who is registered as a payer, that person as a supplier is no longer

liable to register in the country as a payer but instead the reverse charge mechanism will be applied.

- iv Amendment of provisions for the purposes of VAT adjustment in relation to receivables from debtors in insolvency proceedings

The aim is to validate the original intention of the authors of the law, i.e. to enable taxpayers to adjust receivables from debtors in insolvency proceedings in relation to receivables that arose more than 6 months before the court declared insolvency. The amendment of the relevant provision responds to the conclusions of the Supreme Administrative Court, whose judgment interpreted the original, somewhat ambiguous wording of the law in the opposite direction, i.e. that receivables that are 6 months old or less are subject to VAT adjustment.

4. Proposed mitigation of penalties related to the inspection report

The changes approved together with the new Customs Act include the Government's proposal for mitigation of penalties for breach of some duties related to the inspection report.

- || Fines in the fixed amounts of CZK 10,000, CZK 30,000 and CZK 50,000 may be waived on justifiable grounds on the basis of the payer's application, which must be lodged within 3 months of the legal force of the payment assessment.
- || Fines in the amount of CZK 1,000 for a report filed late should be automatically waived once annually for every payer who remedies the shortcoming on his own initiative without being requested to do so by the tax administrator. In addition, fines in this amount arising before the proposed amendment comes into effect will cease to exist by operation of the law, which in the opinion of the Ministry of Finance should retroactively create a transitional tolerance period.
- || Furthermore, it is proposed to prolong the deadline for responding to a request of the tax administrator for clarifying doubts regarding a filed follow-up report from five calendar days to five business days.

5. Information from the General Directorate of Finance on the application of VAT on immovable assets

As we have already informed you, significant changes occur as of 1 January 2016 in the area of the application of exemptions from VAT in the transfer of real estate as a result of an amendment

to the VAT Act. The changes are related primarily to the transfer of land intended for development and transfer of structures after restoration.

Considering that the conditions for exemption from VAT laid down in the new wording of the relevant provisions are formulated relatively vaguely, it is expected that numerous practical questions will need to be addressed. In this context, the General Directorate of Finance has updated its guidance entitled Information on Application of the VAT Act in Relation to Immovable Assets After 1 January 2016 (see <http://www.financnisprava.cz/assets/cs/prilohy/d-seznam-dani/2015-12-21-Informace-nemovitosti-2016.pdf>). In our opinion, however, even by providing this information the General Directorate of Finance did not manage to clarify many questions, but instead achieved the opposite - the guidance tends to make matters even more unclear. Thus, in our opinion, the only way to become better acquainted with the meaning and purpose of the new tax exemption on the transfer of real estate in the VAT Act is through European legislation (specifically the case-law of the Court of Justice of the European Union).

In conclusion, we would like to point out that the new legislation does not apply to transfers of structures acquired before 2013. In relation to such transfers, the original rules of exemption valid before 2013 will continue to be applied. Also, the new legislation does not change the rules for transferring newly constructed structures (for example, flats and private houses), for which value-added tax shall be applied using the well-known method (if the transfer of a flat occurs within three years of issue of the occupancy permit, 21% VAT shall be applied at the output, and a 15% VAT shall apply to structures that are recognised as social housing).

6. Income tax return for the 2015 tax period

The deadline for filing the income tax return for 2015 is approaching. The filing deadline of 1 April 2016 applies to persons and entities that do not have their return prepared by a tax advisor or are not subject to an audit. The basic parameters for preparing the 2015 return remain largely unchanged and only minor changes should be taken into consideration. We summarise some of them below:

Personal income tax

- || As a newly introduced duty, natural persons are obliged to report to the tax authority, within the deadline for filing the tax return, any income which is exempted from tax but has exceeded the amount of CZK 5 million (separately for each source of income). This applies e.g. to exempted income on the sale of property, received donations and inheritance. The reporting duty does not pertain to cases in which the tax administrator can obtain such information from registers or records to which it has access and which it has posted on the official notice board. Failure to comply with the reporting duty is subject to penalties.
- || Newly introduced cap on flat-rate expenditure for taxpayers with income from agricultural produce, forest and water management and payers with income from a vocational trade. Caps for other payer categories remain unchanged.

- || Reinforced conditions for agreements on private life insurance that can be deducted from the tax base and in relation to which employers' contribution will be exempted. This includes, in particular, the impossibility of withdrawing money before the client reaches 60 years of age and before expiry of 60 months of conclusion of the agreement.
- || Increased tax allowance for the second, third and other dependent child (CZK 13,404 for the first child, CZK 15,804 for the second child and CZK 17,004 for the third and all other children).
- || Entitlement to tax allowance for placing a child in a pre-school facility (this was already applied in 2014), up to the amount of CZK 9,200. The definition of pre-school facility is stricter in 2016.

Corporate income tax

- || Application of tax at a reduced rate of 5% only for newly defined basic investment funds.
- || Altered definition of financial leasing in Section 21d of the Income Tax Act. Financial leasing is newly conditional on transfer of liability for the object of the lease (including maintenance and repairs) and risks relating to the object of the lease (e.g. damage) to the lessee (can be applied even to leases in which the object of the lease was handed over after 1 January 2014). The minimum period of the lease corresponds to the minimum depreciation period, where it can be reduced by up to 6 months for assets in depreciation groups 2 to 6 (formerly the reduction was applicable only to depreciation groups 2 and 3; however, for real estate the required period of lease was at least 30 years).
- || Changes in the creation of impairments for receivables arising or payable from 1 January 2014 onwards pursuant to Section 8a of the Provisions Act (the period during which 100% impairment may be created was reduced from 36 to 30 months). The possibility was newly introduced to create impairments for some receivables that were not entered as accounting gains but were taxed (for example, receivables entered through cost reduction).
- || A tax-deductible provision was introduced for the management of waste electrical and electronic waste, which is applicable to entities operating solar panels.
- || The deadline for the payment of additional tax on overdue liabilities was reduced from 36 months to 30 months (it will be applicable to receivables payable after 1 January 2015).

7. Changes related to the audit duty

In connection with the amendment to the Accounting Act, which came into effect at the beginning of this year, some changes were approved in relation to the auditing of financial statements and annual reports.

Already in relation to the auditing of the financial statements for 2015, the auditor had the duty to draw up only a single auditor's report containing all the declarations on the mandatory audit and hence on the annual report. Thus, in practice it will no longer be possible that the auditor's

opinion on the financial statements and on the annual report are issued separately in independent reports.

The duty to have the financial statements audited for periods starting in 2016 will be influenced by several changes in the method of accounting for and reporting certain items. There is a new definition of the concept of "total assets" which is one of the criteria for a mandatory audit and has so far been defined as "gross assets"; it is newly defined as "net assets". The "aggregate annual net turnover" item, which is another criterion for the mandatory audit (and, in addition, for the categorisation of the relevant accounting entity, mandatory consolidation, etc.), will also be subject to changes as a result of a change in accounting for and reporting changes in inventory of own production and capitalisation, which will no longer be included in revenues but accounted for and reported in costs. Thus, for the purposes of determining the duty to have the annual financial statements for 2016 audited, it will be necessary to recalculate the net turnover for the preceding accounting period according to the new content of this item.

A new accounting standard No. 024, "Comparable period for the accounting period starting in 2016", was prepared for the purpose of reporting and comparability of data in the accounting period commencing 1 January 2016 and the preceding accounting period.

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