

New developments in tax legislation

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We would like to inform you about several legislative changes that the second half of 2010 will bring. First we provide several points of the Program Statement of the New Government which show the direction our tax legislation may take in the next years.

At the same time we would like to inform you about several changes that will occur as of 1 January 2011 and the following years. These changes include mainly the amendment to the VAT Act, the introduction of new Tax Rules, the creation of the new finance control offices, and changed standard supply conditions of Incoterms 2010.

Finally would like to inform you about some news relating mainly to individuals, namely the taxation of state bonds, interruption of trade licences, and cancellation of the obligation to keep accounts for photovoltaic projects.

1. Planned changes in the Czech tax system / points from the Governmental Program Statement

At the beginning of August the new Government issued its Program Statement summarising changes it would like to carry out in the coming years. Below we mention the most important points from the Program Statement in relation to taxes.

At the same time there are signals that until the communal and senate elections, which are scheduled to take place between 15 and 16 October 2010, are over we should not expect any significant proposals for tax changes, save for certain exceptions. Our law makers will probably wait until the elections are over.

- Personal income tax or corporate income tax rate will probably not grow. The inheritance and donation tax should become part of the usual income tax. The road tax for personal vehicles may be cancelled.
- The tax system will be simplified and a number of exceptions and allowances will be cancelled. The aim is to tax employment benefits such as meal vouchers, transportation tickets and similar benefits. Employees should be compensated by a single fixed fee which they will be able to deduct regardless of whether they actually apply it or not.
- There should be no limitations to allowances related to: financing own housing (deducted interest from mortgages is still in consideration), families (allowances for children), education, old age savings (additional pension insurance), science and research or support to socially needed.
- The tax burden should shift from direct to indirect taxes. It is almost certain that certain consumer taxation will further gradually increase in relation to alcohol and tobacco.
- For the time being, the Government Program does not include any increases in VAT, or unification of rates. However, due to the financing of the pension reform this will likely happen. The entrepreneurs should not be required to pay VAT for goods and services delivered to companies which did not pay to them for these within a certain period of time.
- The collection and administration of taxes should also be simplified. Due to the creation of unified collection points (for tax and insurance collections), by 2014 we may end up completing only one return rather than three returns. The calculation should be simplified the terms for payments should be unified, and the communication with clerks should be more effective.
- The ability to assess taxes in arrears will extend from the current three to five years. It is planned that there will a general correction duty. Selected clerks should provide a binding interpretation of unclear provisions of law or specific procedures.
- As of 2012 the Government wants to reduce the limits for social security insurance from the multiple of six to the multiple of three of the average wages.
- It is certain that lotteries and any hazard will be taxed more heavily and any exceptions will be removed. Companies carrying out business in this area will be taxed by a unified 20% rate.
- Flat expenses for entrepreneurs and other self-employed persons should not be reduced any more (except for another reduction from 60 to 40% in relation to free trades as approved by the previous senate).

2. Changes from 1 January 2011 and 2012

2.1 Creation of new financial control offices

Two new control offices will be created in the coming years: the General Financial Directorate which will come into existence as of 1 January 2011, and the Specialised Financial Office which will commence its activity as of 1 January 2012. The main purpose for the creation of these offices is the initiative to prevent tax avoidance and better inspection of business entities.

2.1.1 General Financial Directorate

The General Financial Directorate (GFD) with its seat in Prague will be created by separating the Central Financial and Tax Directorate which currently forms part of the Ministry of Finance. This will now be a separate body that will stand between the Ministry of Finance and individual Financial Directorates and that will assume certain functions of the Ministry. The powers of the Ministry of Finance under the Taxes and Fees Administration Act (or in future under the new Tax Rules) will not change.

The main tasks of the GFD will include for example the preparation of new laws, issuance of new tax forms, direction of individual local Financial Directorates, and examination of decisions issued by Financial Directorates.

2.1.2 Specialised Financial Office

The Specialised Financial Office (SFO) will also have its seat in Prague and will be directly subordinated to the Financial Directorate for the capital city of Prague.

The SFO will direct the selected business entities which will meet the law given criteria regardless of their actual place of business. These entities will include bank institutions, insurance companies, re-insurance companies and business entities with a net annual turnover over CZK 2 billion. If the turnover drops under the limit, the SFO's competence will be maintained for the next three years.

Based on the GFD decision these entities may include such entities the administration of which requires certain specialised professional knowledge (for example international companies with transactions involving international taxation, transfer pricing and so on). These complex clients will be serviced by trained specialists. The GFD may also decide that an entity will not be under the SFO's competence although it otherwise meets the prescribed conditions.

In future these new offices should also help to simplify the collection of taxes and insurance.

2.2 Anticipated changes in the area of VAT and Tax Rules

As of 1 January 2011 there will be several changes in the area of VAT. Below we provide a brief overview of the anticipated changes in the VAT Act. We will inform you about the developments of the most important of these changes in our autumn newsletter.

- The time limitation for the reduced tax rate for construction and assembly works related to finished apartments, residential houses and family houses valid only until the end of this year is cancelled. Thus in 2011 the reduced tax rate related to finished housing projects will apply as was the case until today.
- The place of performance in relation to heat and cold supplies will follow the same rules as in the case of electricity and gas supplies by means of supply systems.
- The place of performance in relation to services in culture, art, science, or education events and their organisation (for example exhibitions and fairs) changes in B2B transactions.
- The rules for deducting VAT in relation to long-term assets used in addition to business as well as to non-economic activities will change.
- The correction of the tax base will always be obligatory.
- The option to correct the tax amount in relation to collections from insolvent debtors is introduced.
- The exemption from tax when importing changes.
- VAT will be deducted under stricter conditions (only at the moment a tax document is received and only if the correct entry tax rate is applied).
- Two new law coefficients are introduced.
- The correction period in relation to real estate will be extended to 10 years.
- The technique for correcting and settling deductions changes.
- The institute of tax guarantee is introduced – the joint responsibility of the supplier and customer is introduced in relation to taxable performance for correct VAT payment.
- Special regimes for scrap deliveries, emission permits, construction works and PHM (reverse charge for local supplies) are introduced.

As we have already informed you in our last year's November newsletter please note that there will be new Tax Rules which will take effect as of 1 January 2011 and which will replace the current Taxes and Fees Administration Act. You will find more information on this topic in our newsletter at www.kemphoogstad.com.

2.3 Changes in supply Incoterms conditions

As of 1 January 2011 the international standard supply Incoterms conditions will change. The currently valid standard supply Incoterms 2000 conditions will be replaced by the enhanced Incoterms 2010. In comparison with Incoterms 2000 the supply conditions will be reduced by 2 conditions to 11 conditions, whereas 9 supply conditions will remain unchanged, 4 will be cancelled (DDU, DAF, DES, DEQ) and 2 new conditions will be added (DAT – Delivered at terminal, DAP – Delivered at place).

The supply conditions precisely define the transfer of risks and costs related to the transport of supplied goods between the seller and buyer. The supply conditions are not concerned about the moment the goods ownership is transferred and follow the contractual or payment arrangement.

The contractual parties are not obligated when transporting goods to observe Incoterms and may agree completely individually, but considering that Incoterms have a unified interpretation and are generally known their use contributes to simpler agreements and business arrangements. Supply conditions have a great significance when establishing a customs value of goods because they provide which expenses are included in the price of goods and which are not.

Although the standard supply conditions will change, business partners will be able to use in future the supply conditions which Incoterms 2010 cancel but should not refer to the valid Incoterms 2010 in their agreements.

3. News in particular in relation to individuals

3.1 State bonds

The Ministry of Finance newly can trade in state bonds which only individuals may acquire.

The exemption of these bonds from personal income tax is cancelled and the taxation of the interest yield will be introduced by means of a 15 % withholding tax. The taxation of these bonds will apply even in the case when they are re-purchased or when they are due.

3.2 Interruption of trade licence activities

As of 1 August 2010 the Trades Licensing Act changed in relation to interrupting a trade licence activity. When interrupting a trade licence activity for longer than 6 months, an entrepreneur was required to submit a prior written notice to the Trade Licence Office. The amended Act is more accommodating and allows, but does not order, entrepreneurs to notify about any interruption.

The cancellation of the obligation to notify any interruption of a trade licence activity may relate to a personal income tax base modification. In practise it will probably be possible to carry out a personal income tax base modification only in the case the related interruption is notified.

3.3 Cancellation of the obligation to keep accounts for photovoltaic projects

The Energy Act has also been amended and no longer requires that a trade licence holder be an accounting unit. This cancellation of the obligation to keep accounting may be important in particular in relation to individuals operating photovoltaic power plants who were previously unnecessarily burdened by it.

We trust that you will find most of the prepared legislative changes positive. We will be pleased to discuss any impacts of the above changes on to your company.

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