



# Tax & Legal

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**July 2024**

# Editorial

From our school years, we all certainly remember the moment when it was time to put aside our responsibilities and head out for summer adventures. The beginning of July still holds those special feelings for me, even though my school days are long gone.

This year, summer's more relaxed mood is further enhanced by a recovering economic situation, which has improved for most Czechs for the second year in a row, as it appears that households are slowly getting over the recent economic slump. This is at least what this year's Household Financial Situation Index, KPMG's long-term project in cooperation with STEM, has shown. Nonetheless, we still cannot seem to shake off the bad vibes, as 53 per cent of the people think that the overall situation in the Czech Republic is fairly bleak. Be that as it may, we still expect economic growth to resume this year, and no negative sentiment should hold us back.

In this context, it is a bit of a pity that economic stability and the business environment's predictability are not better supported by the legislator. The new Accounting Act and the accompanying amendment to the Income Tax Act, which, notwithstanding the considerable work in progress and the date on the calendar, have been proposed to take effect as early as 1 January 2025, are (un)successful examples of this.

The current issue of Tax and Legal Update also comments on two judgments of the Supreme Administrative Court relating to income tax, only one of which may, in our opinion, have a positive effect on the stability and predictability of the business environment. For the future, we can only hope that the tax administration and the Czech courts will apply a little bit more common sense.

I sincerely hope that July's Tax and Legal Update will not ruin your good mood. Instead, may you find it an interesting or even inspiring read.

Enjoy your summer.



**Daniel Szmaragowski**

Partner  
KPMG Czech Republic

# Changes to excise duties from 2025

The government has approved a draft amendment to the Excise Duty Act, which introduces several key changes aimed to reduce the administrative burden for taxpayers, increase legal certainty on the market for selected products, and increase the efficiency of the excise duty collection process. The reasons for preparing this amendment are experience from application practice, case law, and the need to respond to new implementing regulations in EU legislation.



**Tomáš Havel**  
thavel@kpmg.cz



**Lukáš Arazim**  
larazim@kpmg.cz

The main motivation for the amendment was the desire to remove legal uncertainties and reduce bureaucracy, which should make it easier for entrepreneurs to do business and at the same time enable tax administrators to administer taxes more efficiently. These changes include, e.g., extending the digitisation of certain processes, which will lead to faster and more transparent communication between taxpayers and tax administrators. However, we will see changes in almost all parts of the law: in some sections these will only be cosmetic and stylistic changes, but in others, these will have an impact on the substance of the law. For example, the amendment changes the assessment and classification of small and independent breweries.

In view of the changes in EU legislation, the amendment aims to significantly streamline the direct collection and refund of excise duties. This includes, e.g., changes to the processes for refunding the excise duty to persons enjoying privileges and immunities, which should greatly simplify and speed up the process. On the other hand, the current deadlines for the refund of the duty on mineral oils to persons using mineral oil for heat production will be shortened: it will only be possible to apply for a refund of excise duty on such oils within three months of the date the entitlement arises, instead of the current six months.

Another area that the amendment is to change is the storage and sale of raw tobacco and the abolition of the 'sell-out period' for cigarettes and heated tobacco products upon a change in the excise duty rate. A relatively welcome change is the reduction of the administrative burden for waste mineral oils: the obligation to prove the economic stability of the applicant for a permit to acquire the selected excise duty-exempt products has been done away with. The conditions for the transport of exempt waste oils will also be amended.

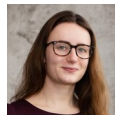
The amendment to the Excise Duty Act thus represents a significant step towards modernising the tax system in line with EU regulations with an impact on tax administration efficiency. It can be expected that the proposed changes, which were also subject to comments by the Chamber of Tax Advisors, will positively affect both the state budget and taxpayers. The draft amendment is currently in the legislative process as Print No. 736 in the chamber of deputies.

# When is an additional VAT return really necessary?

Corrections to already filed VAT returns are not uncommon in practice. Often, we either do not have the tax documents in the period to which they relate or we simply forget to include them. Let's take a look at situations when we are obliged to file an additional VAT return and when we can resolve the corrections more elegantly by including them in the regular VAT return.



**Veronika Výborná**  
vvyborna@kpmg.cz



**Kateřina Zákostelská**  
kzakostelska@kpmg.cz



**Daniela Sommer**  
ddsommer@kpmg.cz

## Section 104 of the VAT Act

Section 104 of the VAT Act deals with incorrect statements of tax for another taxable period. In principle, a VAT payer may declare taxable supplies in a tax return relating to an earlier or later period without having to file an additional VAT return for the period in which the taxable supply should have been included according to the date of supply.

The tax administrator is obliged to accept such a procedure, i.e., they should keep the given supply in the period in which it was reported by the taxpayer.

However, were the inclusion of a fact relevant for determining the tax in the tax return for an earlier taxable period to reduce the tax in that earlier period, the tax administrator shall charge default interest. The same applies to later periods: default interest would be charged if the resulting tax liability were reduced in the taxable period that is correct according to the date of taxable supply. Default interest is payable within 15 days from the date of payment assessment.

Default interest shall not be charged by the tax administrator if the VAT payer declares late supplies received under the reverse charge mechanism and is also fully entitled to the VAT deduction.

Section 104 therefore saves costs both for taxpayers who do not have to file additional tax returns, and for tax administrators who do not have to change previous (or future) tax liabilities by making additional assessments.

## When Section 104 cannot be applied

However, it is not always possible to apply a simplified tax correction procedure. The VAT Act lists situations where taxpayers must file an additional tax return:

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- where the procedure under this provision affects the pro rata or reduction coefficient for the VAT deduction. It is therefore necessary to verify the time shifts at the end of the calendar year.
- where the selected supply is carried out under the OSS scheme with the place of supply in the CR or under the Import OSS scheme.

Furthermore, it is not permissible to include in a tax return for another taxable period facts that relate to the taxable period subject to the procedure to remove doubt or tax inspection.

This basically means that if the taxpayer does not find out about the unreported transactions themselves, but is sent a notice to remove doubts or a tax inspection was initiated against them, the tax administrator will require the filing of an additional tax return.

Finally, please note that all of these procedures can also be used by persons identified for VAT.

# Selected foreigners no longer need work permit from July

The amendment to the Employment Act among other things extended the scope of exemptions from foreigners' obligation to have a relevant permit to work in the Czech Republic: the category 'citizens of selected countries' was added. The government has now adopted a regulation specifying the list of countries to which the exemption will apply from 1 July. For these foreigners, relocating to the Czech Republic will be simplified, although they will still need a residence permit.



**Barbora Cvinerová**  
bcvinerova@kpmg.cz



**Vojtěch Kotora**  
vkotora@kpmg.cz

Generally, foreigners from outside the European Union need an employment permit to work in the Czech Republic. However, selected groups of foreigners who meet specific conditions are exempt from this obligation. These are defined by the Employment Act and include, e.g., holders of permanent residence permits, students or graduates of accredited courses, or holders of certain types of long-term residence permits.

From **1 July**, a new group will be added to the existing exemptions – citizens of selected states. These will automatically gain free access to the Czech labour market, without any further conditions. The government has put on the list of selected countries Australia, Japan, Canada, the Republic of Korea, New Zealand, Great Britain, the United States of America, Singapore, and Israel. The list will probably be expanded in the future to also include citizens of Taiwan, which was dropped from the original proposal because it does not meet the condition of being an independent state. The new free access to the labour market shall apply both to foreigners employed locally and to posted workers.

The obligation to obtain a residence permit remains

Importantly, the described above regulation only concerns work permits. The foreigners will still need to obtain a visa or residence permit to work legally in the Czech Republic. Although all the above countries have visa-free relations with the Czech Republic, i.e., their citizens can stay here for 90 days (and sometimes more) without a visa, this advantage can only be used for non-gainful activity, not for employment or the posting of workers.

In practice, this means that a Schengen visa will still be required for short-term work stays. For long-term stays, i.e., over 3 months, an employee or blue card will be required. Unlike under the current rules, employee cards will be issued to these foreigners under the 'non-dual' regime, and the existing 'dual' employee cards will automatically switch to this regime on 1 July. They will serve only as a residence permit for employment purposes, but the employment itself will no longer be subject to the approval by authorities, neither will any changes of an employer or job (the notification obligation under the Foreigners' Residence Act remains, however). The blue card does not exist in the non-dual regime, and if a foreigner decides to apply for this type of permit, the new regulation will not significantly affect them.

Please note that the need to obtain a residence permit does not only concern foreigners. If a foreigner performs work without a valid residence permit, it is considered illegal employment, for which the employer is liable to

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a fine of up to **CZK 10 million** and other sanctions.

Although free access to the labour market for the above defined foreigners is a significant positive change, **the need to obtain residence permits** will still make their employment more complicated than that of EU citizens. From our discussions with the authorities, we understand that no relaxation of the residence rules is currently being considered.

We have been covering this topic for a long time. We have already reported on the upcoming changes in the employment of foreigners from third countries [here](#), and you can also read about free access to the labour market for foreigners with special long-term residence permits [here](#).

# New way of reporting employees posted to the Czech Republic

The Ministry of Labour and Social Affairs has introduced new rules for the notification of the posting of workers in the Czech Republic within the framework of the transnational provision of services. The rules are effective from 1 July 2024 and apply to all employers who plan to post their employees to the Czech Republic after that date. The new notification system brings several significant changes that will affect the related administrative processes.



**Vojtěch Kotora**  
vkotora@kpmg.cz



**Petr Štětina**  
pstetina@kpmg.cz

## Changes to the notification of postings

From 1 July 2024, all notifications of the commencement of a posting of workers must be made exclusively through a new registration portal launched on 1 July 2024 and managed by the State Labour Inspection Office. New posting notifications made by other means will not be considered valid and will be disregarded.

Since 1 July 2024, the original online form for the commencement or termination of postings as well as the PDF form for the notification of the commencement of a posting are no longer available on the MLSA portal.

## Changes to postings notified by 30 June 2024

Since 1 July 2024, specific rules for posting terminations, extensions or changes apply also to postings that the Labour Office was notified of on or prior to 30 June 2024. Such submissions can now be made in two ways:

1. **New procedure – using the registration portal**; however, this also requires a (retrospective) notification of the commencement of the posting and then the notification of the change or termination.
2. **Transitional procedure – in writing in PDF format**, by sending the completed old form to the relevant branch of the Labour Office of the Czech Republic, as before. This method will be available only until 31 December 2024.

## Employment documentation required

From 1 July 2024, when notifying the posting of their workers, employers must also provide a copy of documents proving the existence of the employment relationship. This documentation must be submitted in Czech or Slovak, or a translation into Czech must be provided by the employer. The employer is then responsible for the accuracy of the translation. Copies of the employment documentation shall be uploaded when registering the posting via the new portal, and any documents must be sent as part of one submission (i.e., sending them separately is inadmissible).

The above changes are part of the state administration's aim to digitise its processes and are intended to simplify

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and streamline the notification of worker postings and to ensure that all relevant data are centrally recorded and easily accessible to the relevant authorities. Employers should pay attention to these new rules to avoid possible sanctions for non-compliance with the notification obligation.

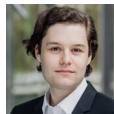
Finally, please note that these changes only apply to postings in the context of the transnational provision of services by an employer established in the EU. Other postings, e.g., from outside the EU, are not subject to these changes and still need to be reported to the Labour Office of the Czech Republic.

# More flexible arrangements for occasional road passenger transport

At the end of May, an EU regulation introducing changes to the rules regarding (minimum) breaks and rest periods in occasional road passenger transport entered into force. The regulation primarily aims to consider the sector's specific working rhythms, ease the rules for drivers in this transport, and thus ensure better services for passengers. The regulation is directly applicable in all member states.



**Lubica Čáp**  
lubicacap@kpmg.cz



**Richard Hajdučík**  
rhajducik@kpmg.cz

Occasional passenger transport means transport that is not regular passenger transport and is usually organised on the initiative of the customer or the transport operator. Examples are recreational, school, or other similar trips. Employers of coach drivers will now be able to split the mandatory breaks or postpone their rest periods.

Under the general legal regulations, drivers must take a break of at least 45 minutes for every 4.5 hours of driving. Occasional drivers will now be able to split this break into two separate periods of at least 15 minutes. At the same time, however, the current requirement that the total break time must be at least 45 minutes shall be maintained.

If drivers are engaged in occasional transport lasting six or more days, they may take their daily rest up to one hour later, provided that the total driving time for that day has not exceeded seven hours. This is subject to the condition that road safety is not jeopardised. It will therefore not be possible to postpone rest every day.

This derogation can only be used on a one-off basis and twice in a single passenger service trip lasting eight days or more. Even in these cases, it will still be necessary to observe the start of the weekly rest period.

To allow for the monitoring of the new derogations, the driver will be required to carry on board the vehicle a journey form completed before the start of the journey, as well as paper or electronic copies of journey forms covering the previous 28 days. The period to be monitored will be extended to 56 days from 31 December 2024. The carrier is not obliged to carry copies if the vehicle uses a tachograph allowing the recording of this type of transport. This is the European Commission's fallback solution until the impending changes to the digital tachograph function are implemented.

Coach drivers will also now be able to drive longer domestic tours of up to 12 days, previously only possible during international trips.

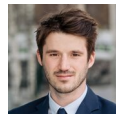
The Commission expects these changes to improve the carriers' ability to organise efficient and high-quality occasional passenger transport, simplify working conditions, and provide greater flexibility for drivers. In practice, adjusting to the new conditions will take some time, and only time will tell what the outcome will be.

# Creditor protection under amendment to Company Conversions Act

On 19 July 2024, a major amendment to the Company Conversions Act (No. 162/2024 Coll.) will enter into effect. In this article, we summarise the changes concerning the protection of creditors and persons participating in the conversion and the exercising of their rights. In this context, we also look into the changes to the information obligations of persons participating in the conversion.



**Petr Janíček**  
pjanicek@kpmg.cz



**Jakub Nováček**  
jnovacek@kpmg.cz

## Providing sufficient security

The amendment to the Company Conversions Act changes the definition of claims where creditors may demand security and the timeframe for exercising the right to security. This also applies to future or contingent claims. Under the literally interpreted previous wording of the act, the protection only applied to outstanding claims that originated before the conversion was recorded in the Commercial Register.

Now, it is explicitly admitted that creditors of future or contingent claims also have a right to sufficient security if the claims arise from obligations originated before the draft terms of the conversion were published and if their recoverability is impaired because of the conversion. This means that claims for which a right to sufficient security arises may not exist at the date of publication of the draft terms of the conversion. The Company Conversions Act thus provides a higher level of protection for creditors of claims arising from long-term contractual relationships (e.g., credit, lease, or general agreements).

For the sake of completeness, we cover changes concerning cross-border company conversions in [this article](#).

If the creditor and the person participating in the conversion do not agree on a method to secure the claim, the creditor must exercise their right to sufficient security before the court within three months of the date of publication of the draft terms of the conversion, otherwise this right ceases to exist. Until now, the time limit was six months from the date of recording the conversion in the Commercial Register. This means that the time limit will be substantially shortened, giving the companies participating in the conversion greater legal certainty. On the other hand, it means that creditors must be more vigilant in protecting their rights. Importantly, the act now explicitly stipulates that the filing of a creditor's petition for sufficient security does not prevent the conversion from being recorded in the Commercial Register.

The amended Company Conversions Act also stipulates that sufficient security shall be established directly by the court's decision. In this context, the amendment explicitly provides for certain aspects of the court proceedings such as the requirement for the creditor to support their reasonable concern, the need for the court to take into account the type and amount of the claim, and the establishment of the security at the earliest as at the date of recording the conversion in the Commercial Register. In practice, the creation of a right of pledge or the provision

of a security deposit may be considered relevant security.

### **Information obligation**

It will also no longer be necessary to publish a notice of the filing of the conversion's draft terms in the Collection of Deeds or to notify creditors of their rights in the Commercial Bulletin. It will now suffice that the person participating in the conversion files a notice to creditors, representatives of employees (or employees), and shareholders/members/partners of their rights in the Collection of Deeds, along with the draft terms of the conversion. The amendment thus simplifies the process of publishing the draft terms of conversions and reduces their financial costs. In practice, in our opinion, the new rule stipulating the obligation to publish the notice of creditor, employee, and shareholder rights also on the participating entity's website, if set up, may be problematic. This rule will affect all joint-stock companies and those limited liability companies (or other corporations) that have voluntarily set up a website. In practice, proving that the notice was published on the company's website for the entire period required by law (one month before the date of approval of the conversion) can be difficult. The extent to which this is necessary and how this shall be proved will only be clarified by practice.

### **Effectiveness of the amendment**

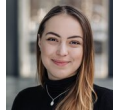
For practice, it is also important which wording of the Company Conversions Act will govern conversions already initiated. The amendment stipulates in its transitional provisions that if the draft terms of the conversion were prepared (i.e., signed) under the version of the law in effect before the amendment's effective date (19 July 2024), the conversion shall be completed in accordance with the law as it currently stands. However, the body of the company competent to approve the conversion may decide (opt-in) that a conversion already in progress should nonetheless proceed in accordance with the new wording of the act.

# Class actions are newly available in the Czech Republic

The closely watched innovative Class Actions Act entered into force on 1 July 2024, making it possible for groups of people to combine their claims based on the same or similar grounds into a single action and save on court costs.



**Pavlína Rampová**  
prampova@kpmg.cz



**Tereza Klabenešová**  
tklabenesova@kpmg.cz

The Act on Collective Civil Proceedings is based on the EU Directive on Representative Actions for the Protection of Collective Interests of Consumers (the RA Directive), requiring the establishment of an effective and efficient procedural mechanism for representative (class) actions to protect the collective interests of consumers (and small businesses), strengthen their position vis-à-vis businesses, and reduce the costs of court proceedings. A summary of the basic elements is provided here:

**What are collective proceedings?** Collective proceedings are court proceedings in which disputes concerning the rights or legitimate interests of several persons are heard and decided upon. This term includes the procedure followed in the proceedings and the enforcement of the decision issued in the proceedings.

**Who does the law apply to?** The act applies to consumer groups. Under the law, the groups can include not just non-business individuals but also small entrepreneurs with up to 10 employees and an annual turnover of up to CZK 50 million.

**How to become a member of a consumer group?** The law is based on an opt-in model. This means that consumers must actively register their claim. A group of at least 10 consumers is required for a class action to be admissible.

**What claims are covered?** The act pertains to claims of the same or similar factual and legal basis, to the extent that it is efficient for the rights and legitimate interests to be heard and decided upon in class proceedings. There is no limitation as to the type and nature of the claim (it is possible to demand, e.g., a monetary compensation, repair/replacement of goods, price reductions, cease and desist orders, the determination of legal relationships). Nor is there any limitation as to the value of the individual performance. However, only disputes concerning rights and legitimate interests that arose after 24 November 2020 shall be heard and decided upon in collective proceedings.

**Who is entitled to bring a class action?** Only non-profit organisations registered with the Ministry of Industry and Trade acting on behalf of a group of consumers (e.g., dTest or the Association of Czech Consumers) can be plaintiffs in the proceedings, and will have to have legal representation.

**How much will it cost to engage in collective proceedings?** There is no charge to join the proceedings. Participating consumers will bear no financial risk should the class action be unsuccessful. However, the plaintiff (a non-profit organisation) in successful proceedings will be entitled to a reasonable fee to be determined by the court. This may not exceed 16% of the adjudicated benefit or CZK 2.5 million if set as a lump sum (especially for non-financial benefits).

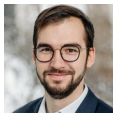
**Which court will decide on the class action?** The competent court of the first instance shall be the Municipal Court in Prague.

**How will the proceedings be conducted?** The procedure can be summarised as follows: (1) a group of at least 10 members with similar claims is assembled, (2) a class action is filed with the court by a non-profit organisation as the plaintiff, (3) the court assesses the admissibility of the class action, (4) the collective proceedings commence, (5) further consumers register their claims within the set deadline, (6) the court decides on the merits.

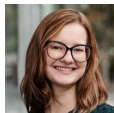
**Where can I find the current proceedings?** The law assumes the establishment of a register of collective proceedings, but this has yet to be made available.

# Obligations under deposit-refund system for PET bottles and cans

Not all PET bottles thrown away in yellow bins are recycled. The mandatory charging of deposits on them should help in this respect. The Ministry of the Environment has published a draft amendment to the Packaging Act. Below we summarise the impact it will have on consumers and businesses.



**Tomáš Kočar**  
tkocar@kpmg.cz



**Karolína Kubíčková**  
kkubickova@kpmg.cz

We informed you about the planned introduction of deposits for PETs and cans in this [previous article](#). The principle of the deposit is that both the producer and the seller will be obliged to add the deposit value on to the amount for which they sell the beverage deposits. To get their deposit back, consumers will have to take the undamaged drink containers, including the label, back to a designated place.

## Drink containers subject to deposit

Deposits will apply to PET containers and cans with content ranging from 0.1 to 3 litres used for soft drinks and some alcoholic beverages containing no more than 15% alcohol. Containers for milk and dairy products, iced coffee with milk, and disposable glass containers will be exempt from this obligation. The same applies to containers provided for transport on international routes (e.g. on buses), sold in duty-free zones, or intended for export.

The deposit amount is still uncertain and will be determined by decree. The Ministry of the Environment estimates it to be at least CZK 4.

## New obligations

New obligations will apply to:

- producers of drink containers
- wholesalers and retailers (i.e., end sellers)
- deposit system operators
- ordinary consumers.

Producers will have to register their containers with an operator and pay a deposit and a fee for each container placed on the market. When the producer sells the beverage in the container subject to deposit to the end seller, the latter will have to pay the deposit in addition to the drink price. Subsequently, the consumer will also pay the end seller a deposit in addition to the price of the drink. When the consumer returns the drink container, the end seller will refund the deposit. The end seller will then return the collected containers to the operator who will refund the relevant deposits. The end seller will in turn pay the operator the handling fee as a reward for handling containers.

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The operator will have several obligations relating to the collected containers, as they will have to check, count, transport and process any waste from the containers. The recycled material can then be resold (e.g. to manufacturers). The life cycle of the material could thus be circular.

In addition, end sellers (regular shops but also petrol stations) will have to set up container take-back points, which in the ministry's estimates may number up to 11,000. In addition to bricks-and-mortar shops, this obligation will also apply to e-shops that have their own delivery (e.g., rohlík.cz or košík.cz).

### **When will the deposit system be launched?**

The ministry originally estimated that the deposit system would start at the beginning of 2025. The bill proposes its effectiveness from 1 January 2025; however, the ministry proposes to allow a year for preparation, with a launch in **2026**. The amendment is now at the beginning of the legislative process and has not yet been submitted to the government for discussion.



# Due Diligence Directive: what companies need to know

The European Union is introducing a new Corporate Sustainability Due Diligence Directive (CSDDD), which introduces new obligations for businesses. Consequently, these should be prepared for greater scrutiny of their activities and their supply chains.



**Tomáš Kočař**  
tkocar@kpmg.cz



**Karolína Kubíčková**  
kkubickova@kpmg.cz

## Obligations for businesses

Companies will have to identify and address the potential and actual negative impacts on human rights and the environment in their operations and in relation to their subsidiaries and business partners. They will therefore need to regularly map risks, take preventive measures to avoid any harm to human rights and the environment, and carry out remedial action when damage occurs.

Furthermore, large companies will be required to develop and implement transition plans to mitigate climate change consistent with the objectives of the Paris Agreement and the European Climate Law.

## Which companies will be covered by the directive?

The directive will apply to large EU companies with more than 500 employees and an annual turnover exceeding EUR 150 million and, under certain conditions, to companies with more than 250 employees and an annual turnover exceeding EUR 40 million. It also applies to large companies from third countries with an annual turnover of more than EUR 150 million in the EU, and under certain conditions even if they have a turnover of more than EUR 40 million.

Micro, small and medium-sized enterprises (SMEs) are not directly covered but may also be indirectly affected as part of large company chains.

## Cost of compliance

To comply with the new obligations, businesses will incur various costs, including the costs of establishing and maintaining mechanisms for risk mapping and management or costs associated with adapting corporate operations and value chains (i.e., activities related to the production of goods or the provision of services, e.g. product development and disposal, and activities in the supplier-customer relationships).

## Enforcing the rules

Member states shall designate the authorities to supervise compliance with the rules and impose penalties for breaches.

Companies will be liable for damage caused by failure to comply with the due diligence obligations. The statutory body shall primarily be responsible for ensuring that legal obligations are complied with. A breach of the relevant obligations could therefore also mean a breach of due managerial care, with all the risks it entails. Victims will be entitled to compensation.

### **Next steps**

The directive will enter into force 20 days after its publication in the Official Journal of the EU. Member states will have two years to transpose it into their national laws. Companies should start working as soon as possible to put the right processes in place to be ready for the new requirements.

The CSDDD represents a fundamental change for businesses in terms of sustainability and human rights. We expect it to affect many related regulations in the Czech Republic. We will keep you informed about any further changes.

# Current developments on Pillar One

The OECD has published additional guidance on setting arm's-length prices of marketing and distribution activities (Amount B) in low-capacity countries (jurisdictions with limited resources and data). The timing of the signing of the multilateral convention has also been clarified.



**Václav Baňka**  
vbanka@kpmg.cz



**David Kronovetr**  
dkronovetr@kpmg.cz

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Pillar One sets rules on how to redistribute a part of profits of the largest and most profitable multinational groups to the countries where their goods are sold or services consumed (Amount A), regardless of their presence in that market country. Pillar One also sets out rules on how to allocate percentage profit margins (Amount B) to marketing and distribution activities in the country of the sale of goods or consumption of services. The rules for determining Amount B should be applicable regardless of the size of the corporate group. They can be found in the OECD's [report](#) of February 2024, which we covered [here](#). Also included are the rules for a simplified and streamlined approach to determine Amount B, which have now been incorporated into the OECD Transfer Pricing Guidelines (Part B, Annex to Chapter IV).

The OECD has released supplementary guidance on the report, with a list of jurisdictions that based on current economic indicators (country rating BBB+ and below) can use this approach, as well as a list of countries that have expressed a preliminary decision to use this option (of large economies, e.g. Brazil, Argentina; of European countries, e.g. Ukraine, Serbia), with the possibility of introducing these rules as early as 2025. The other countries of the Inclusive Framework should respect this approach, so that there should be no further taxation of profits taxed using Amount B in these countries.

At the end of May, the OECD further announced that they are close to finalising all Pillar One documents, with the aim of opening the multilateral convention for signing at the end of June 2024. Several countries are making their commitment to not introduce a digital tax conditional upon implementing Pillar One rules (especially Amount A).

# Pillar Two: Further administrative guidance released

The OECD's Inclusive Framework has issued its fourth administrative guidance on the implementation of the model global minimum tax rules and information on the process of recognising the qualified status of domestic top-up tax.



**Jan Kiss**  
jankiss@kpmg.cz



**Iveta Košťálová**  
ikostalova@kpmg.cz

On 17 June 2024, the OECD published further information on the global minimum (top-up) tax under Pillar Two.

The fourth set of administrative instructions contains unifying information on the following:

- principles for aggregating various categories of deferred tax liabilities to determine whether they have been settled and paid within 5 subsequent taxable periods and therefore there is no need to subsequently reduce the amount of tax included
- methods for determining deferred tax assets and liabilities for the purpose of top-up tax
- allocation of current and deferred cross-border taxes
- rules for allocating profits and taxes in fiscally transparent arrangements
- rules for determining top-up taxes for securitisation vehicles.

In the course of the work on the global minimum tax, the possibility of introducing a domestic top-up tax was added. This will allow profits subject to the minimum tax to be taxed at the level of the jurisdiction in which they are generated and not only at the level of the parent companies. The model rules thus include a specific sequence of steps that prevent a jurisdiction from imposing additional tax on low-taxed group profits where those profits have already been taxed under "qualified" rules in another jurisdiction.

At the same time, a simplified process has been introduced for verifying whether a top-up tax in each jurisdiction is deemed to be qualified. This ensures that tax is levied at the same level as would be levied at the level of the parent companies. The OECD has now published a Q&A document summarising the main features of this transitional qualification mechanism.

# Generous subsidies for industries under EU ETS scheme

The State Environmental Fund of the Czech Republic has announced ENERGETICS No. 1/2024, a new call under the Modernisation Fund focusing on the modernisation of energy sources and production or processing facilities in industries under the EU ETS scheme. Overall, this particular modernisation aims to increase the efficiency of energy sources, reduce energy consumption, and reduce emissions.



**Silvie Beranová**  
sberanova@kpmg.cz



**Monika Svobodová**  
monikasvobodova@kpmg.cz

Companies under the EU ETS scheme can apply for support from 15 July to 15 November 2024 for investments in production that reduce overall energy consumption in industrial installations by at least 20% or greenhouse gas emissions by at least 40%.

The call is intended for entities operating facilities subject to the EU ETS scheme in the territory of the Czech Republic. Funds for allocation are a generous CZK 15 billion. Large businesses can receive support of up to 40% of eligible costs, up to a maximum of CZK 6 billion per project, which must be completed within three years.

Eligible costs include capital expenditure in the form of construction work, supplies of technology or services related to the subject of the aid, as well as costs for technical and author supervision, including OSH, costs for mandatory publicity, etc. Supplies that are to be included in the application for support must be awarded through tenders in accordance with the Public Procurement Act (Act on Public Contracts) / rules for the selection of suppliers.

When submitting their applications, applicants must provide, among other things, emissions and energy assessments requiring, e.g., data on the applicant's energy intensity and emissions over the last five years. On its website, the Ministry of the Environment published a sample model of the required description of the investment and a tool for calculating the aid intensity, titled *Model for Determining the Subsidy Amount – the Ministry of the Environment of the Czech Republic*.

If you are interested in more detailed information, please do not hesitate to contact us. We will be happy to discuss with you your planned modernisation and its chances for obtaining this type of support.

# R&D allowances under TREND programme

The Technology Agency of the Czech Republic has announced the 12th call to participate in the TREND programme focusing on industrial research and experimental development.



**Silvie Beranová**  
sberanova@kpmg.cz



**Lukáš Otýpka**  
lotypka@kpmg.cz

Applications for support can be submitted from 27 June to 14 August 2024. The call is open to businesses that already have experience in their own research and development. Applicants can be small, medium-sized, or large enterprises. Funds for allocation will be determined based on the state budget for 2025.

The maximum aid intensity for large enterprises is limited to between 25% and 65% of eligible costs, depending on whether the enterprise will carry out industrial research or experimental development and whether it will carry out these activities in effective cooperation with an SME or research organisation. Support can be obtained for operating costs. A maximum of CZK 25 million can be awarded per project.

The maximum duration of the project has been set for 36 months, with the deadline for completion of 31 December 2027. At the same time, projects should not start earlier than in January 2025. The project output must be, e.g., an industrial design, utility model, prototype, working sample, software, pilot operation, proven technology, or patent. The lead applicant may submit a maximum of one project proposal. The project can be implemented throughout the Czech Republic (including Prague).

If you are interested, we will be happy to help you with the preparation of your application.

# Amortisation of valuation differences arising on company transformations part of cost base for transfer pricing purposes

The Supreme Administrative Court (SAC) has issued a judgment that may mark a change in the understanding of valuation differences arising on company transformations. Can we expect that Czech administrative courts will take the economic reality into account in transfer pricing in the future?



**Daniel Szmaraowski**  
dszmaragowski@kpmg.cz



**Michala Kopecká**  
mkopeccka@kpmg.cz

In the case at hand, the taxpayer had not included the amortisation of the valuation difference arising from a demerger by spin-off with the creation of a new company in the cost base when calculating the transfer price, or the achieved profitability, to verify that such a price falls within the established margin. The method used was the net profit margin method (TNMM).

Neither the transfer pricing method used (cost plus a mark-up) nor the functional and risk profile of the taxpayer was contested in the dispute. It was 'only' the failure to include the amortisation of the valuation difference in the cost base that was contentious. However, given the amount of the amortisation expense, this was a significant item. Simply put, the tax authorities believed the taxpayer had artificially reduced the price of their products and consequently their tax base by excluding this item. The Supreme Administrative Court sided with the tax administrators who based their reasoning essentially on the fact that the valuation difference was related to the taxpayer's production activities. According to the tax administrator and the SAC, there was no objective reason for excluding the amortisation from the cost base when calculating the profitability of operating costs, as it was an integral part of production costs.

The SAC also emphasised that the tax deductibility of the accounting item in question is not relevant in determining the price of the transaction for transfer pricing purposes. What is relevant is the economic link between the cost in question and the controlled transaction, and not its tax deductibility.

In our opinion, the SAC's conclusion is questionable from a methodological point of view. Firstly, we draw attention to the OECD Guidelines, according to which it is necessary to exclude any items that are not of an operational nature and affect comparability with independent (uncontrolled) transactions. From a transfer pricing perspective, the cost of amortising the valuation difference is not related to a company's operating activities but is essentially an extraordinary accounting item (this is different from recognition in accounting). Secondly, it is important to note that the valuation difference arising on transformations is not and never will be a real expense, but it is 'only' an accounting item that in most cases reflects the future expected profit potential of the spun-off part of a business establishment.

We also believe that the SAC's decision ignores some essential circumstances. For example, while the valuation difference on transformations is accounted for under the Czech accounting regulations and is amortised to expenses over 15 years, under international accounting standards the valuation difference is not recognised and therefore not amortised. Thus, under the SAC's interpretation, applying different accounting standards would thus lead to different results (i.e., a different unit price per product).

The published judgment may also present an interesting paradox in the context of an amendment to the Income Tax Act and the new Accounting Act currently under discussion, as these will allow certain taxpayers to determine their tax base based on accounting records kept in compliance with international accounting regulations.

Another statement of the SAC is also worth noting: in its view, taxpayers cannot bear the consequences of decisions (on mergers) taken by another company in the group and have their profit achieved reduced by the items resulting from such decisions.

### **Consequences of the judgment**

How to read the judgment in question? First of all, it should serve as a caveat of the need to review the transfer pricing calculation setup where a company records goodwill or a valuation difference in its accounts, especially where these accounting items arise from the sale of a business or its part and represent a real expense for the buyer, while the arguments set out above cannot be applied to them. Consideration should also be given to situations where the transfer price excludes certain items that are not taxable/tax deductible. The fact that an expense or revenue is not tax deductible or taxable does not in itself guarantee that the item need not be included in the transfer pricing calculation where cost-based transfer pricing methods are used.



# CJEU on fixed establishment for VAT purposes

In case C 533/22 SC Adient Ltd & Co. KG, the CJEU confirmed its earlier conclusions regarding the origination of a fixed establishment for VAT purposes. In the present case, as in cases C 232/22 Cabot Plastics and C 333/20 Berlin Chemie, the court held that the existence of a passive fixed establishment should not be determined by whether the provider and recipient of the services are part of the same corporate group. At the same time, it confirmed that a passive fixed establishment cannot come into existence based on resources (human and technical) that are identical to those used by the provider to provide services to that establishment.



**Martin Krapinec**  
mkrapinec@kpmg.cz



**Daniela Sommer**  
ddsommer@kpmg.cz

A Romanian supplier to the automotive industry provided manufacturing and related services to its German related party registered for VAT in Romania. The Romanian company applied the general VAT rule and invoiced these services to the recipient's head office in Germany without Romanian VAT. The Romanian tax administration contested this practice on the grounds of an alleged presence of a fixed establishment of the German company, making the Romanian company liable to pay VAT. The case was brought before the Court of Justice of the EU to decide what factors were decisive for the formation of a 'passive' fixed establishment (i.e., a fixed establishment capable of receiving services for VAT purposes).

First, the CJEU stated that the taxation of services at the place of a fixed establishment is an exception to the general rule for determining the place of supply. This exception must be interpreted restrictively and can be applied only if the fixed establishment meets the condition of being equipped with human and technical resources capable of receiving the services for its own needs.

The fact that the two companies belong to the same group or are linked by a contract for the provision of manufacturing services cannot in itself establish a passive fixed establishment for VAT purposes. However, the CJEU stressed that it must be verified that the employees of the service provider are not in fact subordinated to the service recipient in terms of the conditions of their employment and remuneration.

According to the CJEU, even the structure enabling the delivery of goods is not relevant for the existence of a passive fixed establishment. To determine the place of supply of services, it is necessary to consider the structure separately, i.e., solely in terms of its ability to receive and use those services.

Finally, the CJEU held that the existence of a fixed establishment presupposes the use of human and technical resources that are distinct from those used by the service provider. Those resources must be available to the recipient of the services to be able to use them in accordance with their own needs.

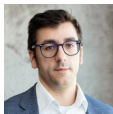
Thus, subject to the verification of the above facts by the referring court, no fixed establishment of the German company originated in Romania for VAT purposes in the present case. When considering the formation of a fixed

establishment, it is always necessary to assess the specific situation, which may vary depending on the contractual relationship and the companies' involvement in the supply chain.

At the same time, we recommend reviewing the related impact on income tax and transfer pricing.

# Supreme Administrative Court defends taxpayer's acquisition structure

The Supreme Administrative Court rejected the tax administration's view that the purchase of a share in a corporation financed by a loan and the subsequent merger to transfer the loan to the newly acquired operating entity constituted an abuse of law. The taxpayer's ability to explain the economic rationale of the transaction contributed to the court's decision in favour of the taxpayer. The requirement of the financing bank to effectively transfer the loan to the operating entity also played an important role.



**Jan Kiss**  
jankiss@kpmg.cz



**Žaneta Pokorná**  
zpokorna@kpmg.cz

The case at hand involved the acquisition of a Czech operating entity by a new investor, a foreign group. The acquisition was followed by intra-group transactions, including a merger which led to the transfer of a bank acquisition loan to the Czech operating entity. This was required by the external bank in the relevant loan documentation.

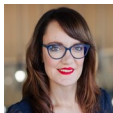
The tax administrator viewed the transfer of the loan to the Czech operating entity by means of a merger (and other transactions) as an abuse of law leading to an unjustified tax advantage (in the form of tax deductible interest on the loan's financing). The tax administrator argued, inter alia, that the transaction could have been arranged in a different manner or that a different transaction could have been carried out.

Both the Regional Court and the Supreme Administrative Court sided with the taxpayer in this case, as they acknowledged that the taxpayer had sufficiently explained the economic rationality of the transactions, with the bank's requirements in the loan agreement playing a key role. According to the SAC, the bank's requirement to transfer the loan to the Czech operating entity was rational because it strengthened the bank's position as a creditor. According to the court, the economic sense of the transaction could not be denied simply by stating that the transaction could have been carried out differently or that a different type of transaction could have been carried out.

We expect this decision to be widely discussed in the future and potentially impact the structure of external acquisitions.

# SAC's Grand Chamber clarifies formal requirements for power of attorney

The Grand Chamber of the Supreme Administrative Court has clarified certain aspects of granting a power of attorney for representation in proceedings before state authorities. The SAC pointed out that there are no stricter requirements for the granting of a power of attorney than it being explicitly accepted by the attorney and granted in a separate deed.



**Jana Fuksová**  
jfuksova@kpmg.cz



**Ondřej Novák**  
ondrejnovak@kpmg.cz

In case [2 As 103\\_2023-47](#), the Grand Chamber of the SAC ruled on whether the acceptance of the power of attorney by the attorney/agent is a condition for the power of attorney to be valid. The question was asked with reference, inter alia, to possible obstructive conduct in connection with authorisation to represent. Both the SAC and the Constitutional Court previously held that where a procedural act is apparently being done on behalf of another, it is the legal obligation of the attorney/agent to prove to the court their authorisation to represent the principal, including their acceptance of the power of attorney. However, this was a specific situation of proceedings with mandatory representation by a lawyer.

According to the SAC, as a rule, a written power of attorney submitted by a party to proceedings need not be executed as a separate deed and need not bear the acceptance clause of the attorney/agent or their signature. If a power of attorney was submitted within another submission, this does not give rise to any doubt as to the representation.

This interpretation means that if there is no doubt as to the power of attorney, then the administrative authority's acts vis-à-vis the representative are effective even if it subsequently turns out that there was no representation in the private law sense. According to this interpretation, even if it is subsequently concluded that there is no contractual relationship establishing a representation, the delivery of notices to such an 'attorney/agent' may still be considered effective – and any negative consequences shall thus be borne by the person who incorrectly identified the attorney/agent.

The reason is that a power of attorney is primarily an external manifestation of the authorisation relationship, vis-à-vis third parties. It is a unilateral act of the principal, as opposed to a legal act which establishes a relationship of representation. The latter is bilateral. This applies throughout the Czech legal system, whereas the former special regulation in the Tax Procedure Code, which explicitly required the acceptance of a power of attorney for tax proceedings, was abandoned as of 1 March 2011. A power of attorney may therefore be contained in any submission by the principal, whether in paper or electronic form, including submissions by data mailbox.

According to the Grand Chamber, the described approach is not an obstacle to sanctioning possible obstructive acts, e.g., if the power of attorney is hidden in the submission as easily overlooked or inconspicuous wording within a large text.

# News in Brief, July 2024

Last month's tax and legal news in one or two sentences.



**Lenka Fialková**  
lfialkova@kpmg.cz



**Václav Baňka**  
vbanka@kpmg.cz

## BRIEFLY FROM HOME

- The GFD has published a position paper to ensure the uniform administration of top-up taxes, which refers to the OECD's previously approved methodological guidance on the global minimum tax. These materials form the basis for EU Council Directive 2022/2523 and Act No. 416/2023 Coll., on top-up taxes. The GFD notes that to maintain uniformity of interpretation and unambiguity of the rules, the documents will not be translated into Czech. The GFD has made clear that it would provide methodological support through expert meetings with taxpayer representatives and professional organisations.
- In its press release, the Ministry of Finance has confirmed its clear intention to extend until 2026 the tax deductibility of aid to Ukraine in the extent provided by Act No. 128/2022 Coll., on tax measures in connection with the armed conflict in the territory of Ukraine caused by the invasion of the Russian Federation.
- The GFD has issued its information on the exemption of income from meals for former employees on a retirement or disability pension from income tax. This non-financial benefit in form of a meal allowance provided to such former employees is exempt from tax up to a limit of CZK 116.20 per calendar day (for 2024) pursuant to Act No. 163/2024 Coll. (consolidation package). The exemption shall apply retroactively from 1 January 2024, which means that employers can make corrections to income tax and insurance prepayments already paid.
- Financial Bulletin No. 5/2024 has disclosed a 'List of contracting states applying the common reporting standard and deadlines' and a 'List for the purposes of fulfilling the information obligation pursuant to Act No. 164/2013 Coll., on International Cooperation in Tax Administration.'

Selected regulations published in the Collection of Laws in June:

- Act No. 163/2024 Coll., amending Act No. 240/2013 Coll., on investment companies and investment funds, and related Decree No. 178/2024 Coll., amending Decree No. 247/2013 Coll., on applications under the Investment Companies and Investment Funds Act.
- Act No. 162/2024 Coll., amending Act No. 125/2008 Coll., on transformations of business companies and cooperatives, as amended, and other related acts.
- Act No. 179/2024 Coll., on collective civil proceedings, and related amendments to other acts.
- Act No. 182/2024 Coll., amending Water Act No. 254/2001 Coll., Act No. 114/1992 Coll., Act on the protection of nature and landscape, and Act No. 465/2023 Coll., amending Act No. 416/2009 Coll., on accelerating the construction of transport, water, energy and electronic communication infrastructure (the Linear Construction Act).
- Government Regulation No. 184/2024 Coll., amending Government Regulation No. 240/2014 Coll., on toll rates and toll discounts and on the procedure for applying toll discounts, as amended.

Relating to labour law, immigration, and other laws under the jurisdiction of the Ministry of Labour and Social Affairs:

- Act No. 152/2024 Coll., on extraordinary waiver of penalties on public health insurance premiums.

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Communication of the Ministry of Labour and Social Affairs No. 177/2024 Coll., announcing the amount corresponding to 50% of the average monthly wage in the national economy for the purposes of the subsistence minimum, and the amount corresponding to 50% and 25% of the average monthly wage in the national economy for the purposes of state social assistance.

- Government Regulation No. 187/2024 Coll. amending Government Regulation No. 220/2019 Coll., on the maximum number of applications for a visa for residence of over 90 days for business purposes, applications for a long-term residence permit for investment purposes, and applications for an employee card that may be submitted at embassies, as amended.
- Government Regulation No. 202/2024 Coll., amending Government Regulation No. 589/2006 Coll., laying down the regulation of working hours and rest periods of employees in transport, as amended, and Government Regulation No. 182/2007 Coll., laying down the specific regulation of working hours and rest periods of members of the fire rescue units of businesses.
- On 1 July 2024, some legislative amendments promoted by the Ministry of Labour and Social Affairs came into force. Inter alia, care allowances have been significantly increased and the mandatory registration of agreements to perform work (outside employment) has been introduced. The Czech Republic is also opening up more to qualified workers from safe countries. Two government regulations proposed by the ministry are also coming into force.
- As of 1 July 2024, amendments to additional pension savings and supplementary pension insurance came into force, changing the amount of state contributions.

Attention should also be paid to the following:

- Deputies have approved an amendment to the Prices Act at third reading. The proposal aims primarily to eliminate cases where the competences of individual pricing authorities to carry out price controls overlap unnecessarily. The main changes include unifying the inconsistent definition of the competence of individual pricing authorities, unifying the rules for issuing price decisions, and unifying terminology across pricing regulations.
- The Ministry of Industry and Trade has prepared an update of the National Artificial Intelligence Strategy (NAIS), which sets priorities and goals in this area until 2030. The key areas of the NAIS are research, development and innovation, education, industry, labour market, ethical, legal and security aspects, public administration, and public services. The updated strategy has been submitted by the ministry to the inter-ministerial comment procedure.

## **BRIEFLY FROM ABROAD**

- On 30 May 2024, Advocate General Juliane Kokott issued her opinion in Case C-432/23. This is yet another decision dealing with the scope of professional confidentiality. The Spanish tax authority asked the Luxembourg authorities for information concerning a Spanish company, to be provided by its Luxembourg lawyer. However, the lawyer refused, pleading professional confidentiality. The Luxembourg Supreme Administrative Court raised a preliminary question regarding the application of professional confidentiality to the exchange of information. According to the Advocate General, services provided by lawyers, including legal advice on matters of company law, are protected by professional confidentiality.

Summary of developments concerning Pillar 2 in selected countries and the EU

- On 29 May 2024, the Belgian tax administration published a decree containing the details on mandatory registration for top-up tax purposes.
- The German Ministry of Finance has published a draft tax return for domestic top-up tax purposes.
- A ministerial decree implementing transitional safe harbours has been published in the Italian Official Bulletin.
- Spain has published a consultation paper on the transposition of the EU Minimum Tax Directive.
- Several Swiss cantons have increased their tax rates with effect from 1 January 2024.
- Guernsey, Jersey, and the Isle of Man have announced the introduction of a qualified domestic minimum

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top-up tax from 1 January 2025.

- The European Commission has called upon six member states (Cyprus, Latvia, Lithuania, Poland, Portugal, and Spain) to transpose the EU Minimum Tax Directive.

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[www.kpmg.cz](http://www.kpmg.cz)

Tel.: +420 222 123 111

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