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Editorial

At first sight it may seem that Czech taxpayers are enjoying a stable tax environment. Changes to tax regulations effective this year are neither extensive nor significant. Even the amendments to the Income Tax Act, Value Added Tax Act and the Tax Procedure Rules, about to enter into effect from April of this year, will not bring any conceptual changes – despite hundreds of individual modifications, often of a technical nature.

Yet, the opposite is true. The tax administration contributes to the instability of the tax environment mainly by changing its approaches, not based on unambiguous changes to legal regulations approved by legislators, but based on additional explanatory amendments to various instructions or notices; these then diametrically alter the tax authority's standpoint. Another way that has become standard is that the Ministry of Finance drafts a bill that passes through all required approval processes. But just when it is almost passed, its original promoter, a/k/a the ministry, comes up with amending proposals or amendments significantly changing the original parameters. Such a perfectly executed somersault, justified solely by the argument that the tax administration should proceed "humanely and with common sense" (!), was demonstrated this week by an amendment to an instruction on VAT ledger statements.

Here I would like to quote the SAC Chairman Josef Baxa, expressing also my wishes for the next election period, both for tax advisors and taxpayers: "The main actors in the political contest should exercise self-restraint, should think of the effects of the changes they are putting through; their effects after they are no longer in power. You cannot change rules halfway through the match just because you are winning and want to secure your victory. Laws must be thought through for hard times, too, and you must not imagine just yourself, with your noble intentions, in power; on the contrary: in your place, you have to imagine someone with different intentions and different qualities. When making rules or changing them, this should be the approach taken. But, sadly, this is not happening. The political rhythm does not bring out long-term considerations, but it is important to feel responsibility not just for oneself, one's party and government, but also for the entire republic, the country."

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Survey: Czech tax environment not supportive of business

Almost two thirds of finance managers do not consider the Czech tax environment favourable for business activities and more than half of them view the changes made in the last two or three years as negative. In their opinion, the most negative is the VAT ledger statement, imposing an even greater administrative burden on corporations. Such are the results of KPMG Czech Republic's survey of 339 finance managers.

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Only 36% of the respondents regard the tax changes of the last two or three years as positive. According to 48%, business entities are most burdened by VAT ledger statements. The electronic reporting of sales (22%) and the separate appendix to income tax returns showing a summary of transactions with related parties (14%) come next. Respondents are in disagreement about the reverse-charge mechanism: more than one third of managers would welcome its implementation on a global basis; in contrast, almost every ninth manager believes that the expansion of the reverse-charge mechanism would be the most burdening tax change in recent years.

Czech finance managers see the highest risk of an additional tax assessment in transfer pricing (41%). In contrast, more than one fifth does not fear any additional assessment of tax; one sixth is worried about their ability to prove the deductibility of their expenses.

According to the survey, the lack of communication with the tax administration is another problem. Only 6% of business entities claim to have learned about changes in tax legislation from the tax administration. One fourth of them would welcome the expansion of binding rulings on any unclear tax issues, which would help them obtain certainty for their future operations. The business environment is developing rapidly, making it very hard to fit new investment and financing concepts into a 1990's tax framework primarily designed for traditional manufacturing companies.

How to deliver data messages with powers of attorney

Delivering messages to data boxes have been causing interpretation uncertainties since 2009 when data boxes were introduced in our legislation, in particular where the formal elements of documents delivered via data boxes are concerned. Both civil and administrative courts have recently expressed their opinion on certain aspects of communication via this system, thus contributing to the creation of a uniform administrative practice.

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In connection with the introduction of the possibility or duty to communicate with public administration via the data box system a number of questions have arisen in practice with respect to the signing and delivery of documents. Early this year, the Supreme Court issued an extensive opinion in which it attempted to harmonise the courts' approach to the sending of messages through data boxes. It confirmed, *inter alia*, that where an entity performs a submission in form of an appendix to a data message (in PDF format, for example), this appendix need not be signed by an acceptable electronic signature.

The above applies unless it is clear from the submission that although the data message was sent by one entity, the message actually relates to another entity and the data message itself is only a medium or an envelope. The submission then should be attributed to the entity that is the actual author. If, for example, Mr Novák files an appeal via a data message that is signed by his friend Mr Svoboda's acceptable electronic signature (e.g. as he deems this to be the quickest way of delivery), the court should regard this document as Mr Svoboda's appeal.

Where an individual has more than one data box (e.g. one as a person not carrying out business activities and one as a lawyer), the state body should always deliver to the data box that corresponds to the nature of the document. For example, a decision to impose a fine for fast driving should be delivered to a private data box and not to the person's professional data box. But, even if such an error occurs, the message is considered delivered in due manner, i.e. at the moment the addressee accesses their data box, the document is deemed delivered.

Even though the above conclusions are *a priori* applicable to civil court proceedings, administrative courts are often inspired by the general courts and *vice versa*. Moreover, it cannot be excluded that these conclusions will also be applied to tax matters. In its opinion following civil proceedings, the Supreme Administrative Court recently held that the confirmation of delivery to a data box is a public instrument associated with the presumption of accuracy. Consequently, if anybody attempts to challenge the accuracy of this confirmation, they have to prove so in a credible manner.

As regards delivery, the SAC recently also confirmed that the rules on observing a deadline under the Tax Procedure Rules should also apply to powers of attorney granted to tax advisors, which means that it is sufficient to submit a power of attorney for delivery by post on the last day of the deadline. Despite the fact that a large number of processes in communication with the tax administration have been digitalised, the tax authorities still insist on the submission of powers of attorney in written form.

GFD provides clarification on reporting of sales received from carriers

Have you properly set contractual terms and conditions with your carriers? Do you know when and who is supposed to report sales with payment collection provided by carriers? Please note that for ERS purposes, not all carriers are the same! The General Financial Directorate published material providing guidance to taxpayers on the reporting of sales these taxpayers receive via carriers. This does not only apply to e-shops but also to all that dispatch their goods via carriers, if these receive payments for the goods they deliver.

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If you use external carriers, messengers or post service providers ("carriers" in general) for the dispatch of your goods and collection of your payments, you should review whether the contractual relationships with the carriers and the relevant reporting of sales comply with the Act on Electronic Reporting of Sales and the GFD's interpretations.

Most important and decisive is the title under which the carrier receives payments from customers. In practice, there are generally three contractual scenarios: direct representation, indirect representation and a special mediation category. Simultaneously, the GDF emphasises that the contractual relationship's content and not just its formal designation is crucial in this respect.

Where carriers collect sales based on contracts for direct representation (e.g. contracts of mandate), they act on behalf and on the account of the appropriate taxpayer/seller. Such payments must be reported no later than at the moment the carrier accepts the payment from the end customer. Taxpayers/sellers are responsible for the reporting of sales or they may place their ERS certificates into the custody of the carriers. Another option is to authorise the carrier to report these sales. The receipt's essential elements will depend on the selected reporting method, as these elements may differ each time.

Where carriers act based on contracts for indirect representation (e.g. consignment contracts), i.e. when they act in their own name but on the taxpayer's account, the received payment must also be reported no later than at the moment the carrier accepts the payment. Unlike for direct representation, the payment is reported by the carrier using their own ERS certificate. Here, the receipt's essential elements vary from the essential elements pertaining to the previous scenario.

Transactions during which carriers act as mediators, in particular post service operators included in a listing published by the Czech Telecommunication Office, form a separate category. It should be noted here that, at variance with information included in the methodological guidance on the electronic reporting of sales, the GFD specifies other situations in which carriers other than post service operators act as mediators. During these transactions, sales must be reported the moment the carrier hands over/transfers the payment to the taxpayer. Where payments using credit cards are concerned, the GFD's already-published opinion on payments made via payment terminals must be taken into account.

Amendment significantly expands reporting duties towards tax authority

In mid-February, the Ministry of Finance submitted an amendment to the Tax Procedure Rules for an accelerated comment procedure. This amendment should ensure access to other information about taxable entities and their bank accounts to tax and other state authorities, responding to a recent decision on the scope of banks' reporting duties.

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It is clear from the ministry's explanatory report that it does not agree with the Supreme Administrative Court's restriction of the scope of information provided by banks and other similar institutions to information explicitly specified in the Tax Procedure Rules. Under the new amendment, information that upon request will have to be submitted to the tax authority will also include information about persons authorised to dispose of cash at the bank, persons who deposited cash to an account and about payment recipients. It will also include information about remote access services attached to a bank account, including specifics of the remote access equipment, and information about safe deposit boxes.

Referring to the EU Directive on Administrative Cooperation (DAC 5), the ministry proposes to extend the catalogue of information submitted by liable persons under the Act on Some Measures against Legalisation of Proceeds from Criminal Activity and Financing of Terrorism (the Anti-Money Laundering Act). In accordance with the new amendment, the tax authority will be able to request from various entities all information obtained during the identification and inspection of clients under the act, including related written materials and information about the collection method of such information. Currently, only the Financial Intelligence Authority (since 2017, the successor to the Ministry of Finance's financial intelligence department) has this information at its disposal. The amendment should primarily affect professions where confidentiality is protected by special regulations. In addition to banks and other financial institutions, this mainly involves notaries, attorneys-at-law, bailiffs, tax advisors as well as real estate brokers and used car dealers. The ministry's proposal caused much outrage among professional chambers, asserting a conflict with their pledge of confidentiality.

Clarification of VAT regime on re-sale of telecommunication services

The General Financial Directorate (GFD) decided to respond to frequent inquiries regarding the purchase and sale of electronic communication services and issued a clarifying appendix to its already-published information. The application of a different regime before the appendix's effective date should not be challenged by the financial administration if the regime has been applied in good faith and in mutual agreement of both parties.

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The first part of the appendix specifies the conditions that must be met to apply the reverse-charge mechanism. The second part describes specific examples. Apart from a basic condition under which both the service provider and the service recipient must be VAT payers, the appendix points out that both parties to a transaction must also operate in the electronic communication sector. A business entity is an entity that purchases services with the intention of subsequently selling them for profit (no matter whether it succeeds). An increase of the price by potentially necessary administrative costs associated with the re-sale is not considered an intention to generate profit.

Consequently, a relatively narrow group of transactions is subject to the reverse-charge mechanism. The purchase of electronic communication services by one mobile operator from another mobile operator and their subsequent re-sale to generate profit is a typical example to which the reverse-charge mechanism applies.

In contrast, the purchase of telecommunication services from an operator for its own consumption or for the purpose of allowing other end users to consume these services will be invoiced by the operator including VAT (i.e. the reverse-charge regime does not apply). These involve purchases of telecommunication services by:

- employers who subsequently re-invoice private calls to employees without a margin;
- parent companies that subsequently re-invoice part of these services to their subsidiaries without a margin;
- municipalities that subsequently re-invoice the purchase price of these services to nursery schools;
- owners of real property who re-invoice these services to lessees along with lease payments without a margin;
- airport operators who provide free-of-charge access to Wi-Fi connections to passengers.

The reverse-charge mechanism should be applied to the taxable supply as a whole in cases where a business entity operating in electronic communications purchases telecommunication services for both its own consumption and to allow other end users to consume the services and to re-sell the services for profit. To enhance certainty, the GFD recommends operators request written declarations from service recipients confirming the purpose for which telecommunication services are procured.

Where the application of a VAT regime in a specific case is disputable, it is possible to use the legal fiction that the supply is subject to the reverse-charge regime, but only if the regime is applied by both parties. It is also possible to apply for a binding ruling by the GFD.

EU taking a closer look at cross-border posting of workers

Within cross-border provisions of services, many entrepreneurs post their employees to temporarily work in other EU countries. As the services' users in economically stronger member states might easily misuse cheaper labour from abroad, since 1996 the EU has been regulating the conditions that must be guaranteed to workers posted abroad. Some employers, however, have found ways to circumvent the regulation, which is why the EU has adopted a new directive aimed at better enforcing the existing duties. Its implementation in Czech law is taking place through amendments to three separate acts, which are now going to the senate.

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In accordance with the original directive on posting workers aboard, the Czech Labour Code stipulates that employees posted to work in the Czech Republic by an employer with its registered office in another EU country must be guaranteed at least the basic Czech working conditions by the posting employer if they are more advantageous for the employees. This minimum standard concerns working hours and holidays, minimum and guaranteed wages including extra pay for overtime, occupational safety and health protection regulation, working condition of pregnant and breast-feeding employees and minor-aged employees, equal treatment and non-discrimination of employees, and, finally, working conditions of agency employees. The labour laws of the other member states then similarly protect Czech employees posted to work abroad.

Nevertheless, the practical application of the directive has lagged behind. The new directive thus aims to establish a more efficient monitoring system of compliance with the stipulated duties. The Ministry of Labour implements the new directive through amendments to the Labour Inspection Act, the Labour Code and the Employment Act. The amendments are now going through the legislative process, and their wording has already been passed by the chamber of deputies.

Under the amended Labour Code, a Czech company as a foreign supplier's customer should also be liable for making sure that employees posted to it receive remuneration at least equal to Czech minimum limits. At the same time, the powers of the Labour Inspection Office are being extended: it will be authorised to check whether employers are truthfully declaring the originating country of the employees, whether the posting is indeed temporary, and whether minimum standards are being guaranteed to the employees. And offenders will not be able to hide behind state borders: national authorities supervising compliance with labour laws will closely cooperate.

Czech employers posting their employees to work abroad have to expect that the inspection authorities of other member states will apply a similarly stricter regime. To allow for the employers' better orientation in working conditions abroad, all national inspection authorities will be obliged to publish all relevant rules online.

Banks fighting cyber threats jointly

The Ministry of Finance is preparing an amendment to the Act on Banks and the Act on Savings and Credit Unions. Its primary purpose is to modify these laws according to changes that have been made to related legislation. Additionally, a new information database will come into existence to help banks to better inform each other on cyber security incidents and on measures taken to address them. The aim of all the actions is to enhance the prevention of cyber-attacks and to minimise potential losses.

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The implementation of the information database follows a regulation in the Cyber Security Act, imposing on selected entities a duty to report, without delay, any cyber security incidents; this means any breach of information security in an information system, for example, the detection of fraud through the misuse of access passwords to internet banking. The database will be accessible to all banks, branches of foreign banks and the Czech National Bank. Of course, the banks will be obliged to keep confidential any information gathered from the database.

The purpose is to improve the banks' awareness regarding possible cyber threats and to encourage their cooperation in addressing them. Experience has shown that once an attacker has attempted to compromise one bank's system in a certain way, similar attempts to access other banks can be expected. The banks should also share information on the measures adopted to address such cyber security incidents within 30 days after their detection. Notably, the act does not stipulate a duty to always accept and implement a certain measure; this will always depend on the nature of the attack and other circumstances.

The amendment also extends the information duty vis-a-vis customers; introduces a new remedy in the form of a duty to replace the auditor; simplifies cross-border business for credit institutions; and reflects new reasons for lifting bank secrecy under the Act on the Police of the Czech Republic and the Act on the General Inspection of Security Forces. The wording of the amendment has not yet been approved by the government, which means that it still may change. The effective date is planned for 3 January 2018, the above described information database should start functioning from 1 January 2019.

Amendment to the Building Act simplifies construction permits

An amendment to the Building Act has passed its second reading in the Chamber of Deputies. The main change that it brings is the new concept of a joint zoning and building procedure, including the possibility to issue a joint ruling for such a procedure. The amendment envisages other changes as well. If adopted, the amended act will make obtaining a building permit easier and faster.

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The new act contains a number of novelties in construction law. Undoubtedly, the most significant one is the possibility of combining a town and country planning (zoning) procedure and a building procedure into a single, joint procedure, whose result would be a coordinated permit, placing and at the same time permitting the construction. A binding assessment of the environmental impact of the construction, forming the basis for permit issuance, would also be integrated in the joint permit.

The joint permit concept is not the only expected change. Affected authorities will now have to publish town and country planning (zoning) documentation on the internet. When updating or modifying planning (zoning) documentation, a precondition of its effectiveness will be the publishing of the complete updated or modified document. This should contribute to higher transparency and better orientation in the building procedure. Furthermore, municipal councils will no longer have to obtain a separate town and country (zoning) plan and a regulatory plan. Instead, they could adopt a unified town and country plan with elements of a regulatory plan. This measure of a general nature could then be reviewed or cancelled within one year from its effective date at the latest.

The proposed amendment also contains the principles of the so far unpassed Line Structures Act (regulating for instance roads, railways). Should it not be objectively possible to place a line structure in the corridor intended for it in the town and country plan, for instance on the grounds of geological research carried out, the relevant regional authority could in undeveloped areas decide on diverting from such corridor. As a result, the foundations for a high-speed rail not only from Prague to Brno, but also for instance from Prague to Dresden may be laid within the next 20 years. Apart from fundamental issues, such as the mentioned line structures, the amendment also addresses the day-to-day problems of citizens: for instance, it will no longer be necessary to obtain the consent of one's neighbour to build a fence higher than 2 meters.

According to the promoters' vision, the changes should simplify and speed-up the obtention of building permits, reduce the administrative burden and increase applicants' ability to compete. Investment construction should also be encouraged. The existing process of obtaining all necessary permits for construction can be described as fragmented and overly complex. The adoption of the amendment would thus be a welcome change, with the potential, among others, to encourage the desired development of infrastructure.

OECD makes blanket change to double tax treaties

In November 2016, OECD released a multilateral convention that will affect the application of double tax treaties. The instrument implements the outcomes of the BEPS Action Plan into more than 2 000 tax treaties. A signing ceremony has been planned for July of this year in Paris. The multilateral convention proposes measures in four basic areas: neutralising the effects of hybrid mismatches; preventing tax treaty abuse; avoidance of permanent establishment status; and resolution of treaty-related disputes.

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Individual states will have to implement provisions to prevent entities from using tax treaties primarily to reduce their tax base. The multilateral convention offers numerous ways to achieve this. The simplest way, and the one likely to be preferred by many states, is the implementation of a 'principal purpose test' – the entity will not be allowed to apply the tax treaty if it is obvious that obtaining the benefit was one of the principal purposes of a transaction or arrangement. Above this basic rule, the states may also choose to apply a 'Limitation of Benefits' provision. This means that an entity would have to comply with detailed conditions to apply a tax treaty. Historically, such provisions have been a part of the double tax treaty between the Czech Republic and the U.S., for instance.

The states that join the multilateral convention also have to adopt measures regarding the resolution of disputes arising from double tax treaties. For instance, within a period of three years, a taxpayer believing tax withheld abroad to be at variance with the relevant tax treaty could apply for a review with a tax administrator in any one of the two states. Individual states will then have to attempt to settle the issue by mutual agreement; where an agreement is not reached, arbitration may follow.

Measures against hybrid mismatches address, e.g., the taxation of fiscally transparent entities, dual residency issues, and the application of methods for the elimination of double taxation where a payment reduces the tax base in one country but is not taxed in the other country. As for permanent establishments, the multilateral instrument stipulates, among others, the rules regarding commissionaire arrangements, activities of a preparatory or auxiliary character, and the time test for the origination of a permanent establishment. Neither the rules against hybrid mismatches nor the rules regarding permanent establishments are obligatory, meaning that the states may decide not to implement the proposed measures.

Although the Czech Republic has yet to issue its official standpoint, it is expected to join the multilateral convention. The instrument will thus also affect Czech entities with foreign business relations. At the moment it is not clear whether the Czech Republic will choose the 'minimum standard' approach and only accept the obligatory provisions (basically, the principal purpose test and the dispute resolution provision), or whether it will opt for a more extensive implementation.

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How to keep R&D expense records separate

To claim a research and development deduction in a tax return, taxpayers have to correctly assess the activities, prepare a project documentation, and properly record related expenses, separately from other costs. But what exactly does such separate record-keeping entail?

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Court decisions on tax deductions for research and development have been growing in number. So far, however, case law has mostly dealt with the differentiation of research and development activities from innovations, or with required project documentation essentials. Recently, however, the Supreme Administrative Court (SAC) in judgement 9 Afs 144/2016-51 dealt with the manner of recording personnel and operating expenses relating to research and development, including supporting (proving) that they actually have been incurred.

In the case in question, a taxpayer recorded expenses on research and development projects in sub-ledger accounts, not using the option to record the expenses through 'cost centres'. The accounting records thus did not contain a direct link to specific development projects. The record-keeping of personnel expenses for employees working on the development projects consisted in a plan of percentage share in the employees' total working hours. The plan was part of the project documentation and prepared prior to the development activities. The tax administrator challenged this expense record-keeping manner as insufficiently supportable and argued that the condition of keeping separate records of expenses had not been met. This resulted in additional tax assessment based on a rejected tax deduction claim.

The SAC fully sided with the tax administrator, stating that the determination of hours worked solely as a percentage of total hours did not at all support (prove) that the employees actually had devoted any time to the development project. According to the SAC, records have to be kept in a manner specifying the employee's activities, when such activities were carried out, and demonstrating a direct link to research and development activities.

The SAC held that its perceived purpose of separate record keeping is to create a complete inventory of all expenses incurred in the implementation of a research and development project. It also emphasised that expenses in the separate records must be identified in a manner that will link individual accounting documents to the recorded expenses. The SAC did not specify which exact manner of keeping records would comply with its understanding of separate record keeping (i.e. whether accounting through cost centres would be acceptable). Using the SAC's words: expenses in the separate records must be sufficiently specified and reflect reality.

It is thus advisable to devote proper attention to the manner of recording expenses for research and development projects. We will be happy to assist you in setting up a separate record-keeping system.

When is a corporation not criminally liable?

At the end of last year, the Supreme Court opined on the limits of corporate criminal liability. Case law in this field has been quite sporadic. In regards to last December's amendment to the Corporate Criminal Liability Act, any ruling that interprets the Act's ambiguities is certainly welcome. Apart from court decisions, there is another helpful tool: a guide through new legislation for public prosecutors, prepared by the Supreme Public Prosecutor's Office.

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Apart from extending the number of offences that corporations may be liable for, the amendment to the Corporate Criminal Liability Act also introduced a new concept of exoneration. Corporate entities have thus been busy revising or redesigning compliance mechanism that may serve to exonerate them from criminal liability. The Act, however, does not provide exact guidelines as to what measures should be adopted. The Supreme Public Prosecutor's Office thus has taken the initiative and published a methodological guide on how public prosecutors should proceed when applying the provision on a corporate entity's exoneration. This is a useful document, emphasizing primarily corporate culture and suggesting how to assess the setup and effectiveness of compliance programmes.

Late last year, the Supreme Court also opined on the corporate criminal liability in a case regarding credit fraud. In the case in question, the court held that where an individual commits an offence in a corporation's name or as part of its activity, but actually to the detriment of the corporation, the offence should not be attributed to the corporation. In such cases, the court held that it is not the purpose of the law to apply criminal liability against the corporation; despite the otherwise generally applicable principle that a corporate entity is liable for choosing the persons authorised to act on its behalf and for persons acting on its behalf.

According to the court, it is necessary to consider the nature of the criminal act and the intention of the person acting, as well as the action on behalf of the corporation within the criminal act that is to be attributed to it, in particular when considering the excesses of persons acting on behalf of a corporation, as described above. In principle, if the act has been committed against the corporation's interest or to its detriment (harm), any criminal liability of the corporation thus harmed cannot be inferred and in such a case, only the criminal liability of the person acting will apply.

This Supreme Court decision is another piece in the case law mosaic of corporate criminal liability. The conclusion that acts pursuing solely personal interests of individuals who knowingly and deliberately take advantage of a corporation cannot be attributed to the corporation is only to be welcome. The same goes for the Supreme Public Prosecutor's Office's methodological guide, bound to become highly useful.

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Consideration for transfer of technical improvement – good news on the horizon?

In the autumn of 2014, the Supreme Administrative Court's ruling, stating that the right to carry out tax depreciation of a technical improvement cannot be transferred between tenants, stirred the tax waters considerably. The case has now returned to the SAC, which, through the perspective of another panel of judges, admitted a certain shift in its interpretation. This gives taxpayers new hope that transfers of technical improvements for consideration will be treated more favourably from a tax perspective.

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Let us briefly recapitulate the background: a tenant carried out a loan-financed technical improvement of a leased building. Subsequently, the lease was ceded (transferred) and the original and the new tenant concluded an agreement on the settlement of rights and obligations. The transfer of the technical improvement and of the liability arising from a portion of the loan were part of the agreement, as was consideration for both transfers. The new tenant then depreciated the thus acquired technical improvement for tax purposes.

In its original judgement, the SAC closed the entire matter by stating that it was not possible to transfer the right to depreciate technical improvement. The payment for the transfer of the technical improvement could hence not be treated as a taxable supply. The new tenant thus did not have an entitlement to deduct VAT on entry.

The subsequent judgement of the second panel of judges published under No. 2 Afs 62/2015-28 fully agreed with the conclusion that the right to carry out the tax depreciation of a technical improvement cannot be transferred between tenants, and that the depreciation of the technical improvement can only be finished by the owner of the real property. However, the second panel presented a slightly different view of the matter, giving its opinion on the nature of the consideration negotiated between the two tenants. In the case in question, the consideration was negotiated for two supplies – assistance services regarding the transfer of the liability arising from the part of the loan (the original tenant was to play the role of "financial buffer" between the new tenant and the creditor) on one hand, and the transfer of the technical improvement itself (consideration equal to its net book value) on the other.

As for the consideration for the first supply, the SAC used an example to demonstrate that a rational relationship does not always have to be direct, and may operate as a chain of relationships. For instance, the relationship between the original and the new tenant may consist of ensuring the undisturbed factual use and operation of the premises, which will serve to generate income. In other words, the negotiated consideration for the assistance service, in the specified scope, may have an economic logic and sense, according to the court. If economic substance is proved, a taxable supply may be the case.

As for the transfer of the technical improvement, the SAC concluded that the supply between the original and the new tenant arising from a private-law agreement on the transfer of rights and obligations from a lease agreement

should be treated as a tax deductible expense (subject to meeting the statutory condition of the expense being incurred to generate, secure and maintain income). According to the SAC, in these cases the transfer of the technical improvement should be viewed as a transfer of a functional economic unit, although no transfer in terms of ownership title has taken place. In this case as well, the SAC emphasized that the transfer must have a proper economic substance. Let us hope that the court thus have indicated a future shift in the tax administrators' approach to this issue.

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SAC on VAT exemption

In tax inspections, tax offices increasingly focus on VAT fraud connected with the transit of goods. What to watch out for when delivering goods to another EU member state, and how not raise the tax authority's suspicions? The recent Supreme Administrative Court ruling may help with the answers.

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In Supreme Administrative Court (SAC) judgement No. 9 Afs 48/2016, a company delivered goods to Germany and claimed VAT exemption in accordance with the relevant provision of the VAT Act. The tax administrator, however, ascertained that in several consecutive cases of delivery, the goods were actually unloaded in Ireland, a different state than the one declared by the company. Ireland was also stated in the international transport notes. The company was thus denied the entitlement for VAT exemption.

Under the VAT Act, three conditions have to be cumulatively met for the entitlement to an exemption from exit VAT to arise: the first condition is that the goods are delivered to another member state to a person registered for tax in another member state. The second condition is that goods are dispatched or transported to another member state. This is connected with the third condition, stipulating that the transportation of goods must be provided for by the payer or acquirer, or a third person authorised to do so.

In this case, the company referred to the Court of Justice of the EU's ruling in the Teleos case. This judgement defined the conditions for VAT exemption for intra-community deliveries and dealt with the possibility of substituting any of the evidence by claiming good faith. The SAC nevertheless refused to acknowledge that the company might have been acting in good faith, since it knew that the goods were being transported to a different state than had been contracted, even though the company's representative had personally met with the customer and checked his registration in the VIES system. The SAC noted that the company should have had substantial doubts as to the place of delivery and should have requested further evidence that the goods had been delivered to the contractual customer. According to the SAC, the situation was thus completely different from the Teleos judgement. The conditions for VAT exemption were not met, and the good faith of the company was not proved. The supply was eventually classified as a local supply, and the company was obliged to report exit VAT on the supply.

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