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In brief

News in brief, August 2024

Editorial

In my editorial for the August issue of Tax and Legal Update, I would like to recommend some reading for the second half of the summer season. So, what to peruse on the beach, by the river, or in the mountains? The offer is very broad this year.

A major amendment to the VAT Act will change the VAT treatment of supply of immovable property and the method of correcting the tax base for bad debts, among other things. The world of VAT will not be the same.

Also worth noting is the amendment to the Act on Top-Up Tax. Among other things, it aims to ensure that Czech top-up tax will be regarded as qualified for permanent safe harbour purposes. Hence, good news for all fans of Pillar 2 and safe harbours.

The amendment to the Income Tax Act, which accompanies the forthcoming Accounting Act, is the heaviest read. Unless you are a tax masochist, you'd better leave it till after the holidays. The amendment harbours numerous changes, with 67 pages of comments from the Chamber of Tax Advisers alone.

We have already discussed the impact of this amendment on companies, so I will just mention that several of the changes bear a positive potential for taxpayers - e.g. the increase in the asset limit to CZK 100,000, the abolition of depreciation groups, the creation of adjustments for tax purposes independent of accounting, or the possibility to use IFRS as a starting point for tax calculation. Unfortunately, due to the need to adjust the tax base for permanent differences between IFRS and CAS, it will still be necessary to keep records of the differences between the two standards. Some of the amendment's shortcomings will hopefully be corrected during its debate.

The amendment will significantly affect both legal entities and natural persons. One of the most debated points is the introduction of the concept of a 'registered asset' instead of the existing 'business property'. This has raised concerns that for individuals, it will lead to a narrowing of the scope of tax exemptions. The Ministry of Finance has already promised a remedy, so let's hope for the best.

Once you finish reading all the holiday "bestsellers", we can start getting ready for the kids going back to school, and also for our regular relay race. You are cordially invited to join us for the third annual KPMG Extra Mile on 19 September. It will once again be a great opportunity to meet, play sports, and have fun outside the office. We are looking forward to seeing you there!

Have a nice rest of the summer.



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Amendment to Income Tax Act introduces huge changes in personal income tax

Responding to the forthcoming new Accounting Act, the Ministry of Finance has published a draft amendment to the Income Tax Act. The proposed effective date of 1 January 2025 and other parts of the amendment may still change during the legislative process.



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We discussed the impact of the amendment on corporate income tax in our June Tax and Legal Update. However, the amendment also has a very significant impact on personal income tax, as many provisions of the Income Tax Act apply to both legal entities and individuals. Moreover, the overall concept of the Income Tax Act is to change. Below, we discuss selected changes that will significantly affect individuals (natural persons).

Tax asset

For individuals, the definition of 'business property' will be abolished following the newly introduced accounting concept of **'asset'**.

Currently, for tax purposes, the business property of a taxpayer who is an individual is considered to be the portion of the taxpayer's property that has been or is being accounted for or included in their tax records. The taxpayer does not have any business property if they claim expenses as a percentage of income or if the property is leased. Whether the taxpayer has or does not have business property then has implications on the taxation and tax exemption of income from the sale of such property. The tax exemption is subject to a time test (10 years; 5 years for real property acquired before the end of 2020) from the moment of the acquisition of the real property and not from the moment of the disposal of the real property from the business property. And this is just one of the most common examples where this approach is applied.

The amendment completely changes the basic principles described above. For tax purposes, a new concept of 'registered asset' is introduced. This is to be **an asset which the taxpayer has entered in their tax records or which is crucial for generating the taxpayer's taxable income** (i.e., rental income or income from self-employment where the taxpayer claims expenses as a fixed percentage, but also income by taxpayers under the lump-sum tax regime). The decisive factor is the factual state and purpose of the asset, i.e., whether the use of the asset is crucial for generating the taxpayer's taxable income and not whether the asset is registered in their tax records. Its disposal should be the point at which the registered asset ceases to be an asset of the taxpayer. For a better understanding of the provision in question, it is necessary to look at the explanatory report, which states that this point in time will be considered to be, e.g., the sale of the asset in question. In other words, even if the real property has not been leased by the taxpayer for several years, it will still be considered a registered asset until sold.

The taxpayer who claims (deducts) actual expenses (instead of a fixed percentage) may choose not to register an asset in their tax records even if the asset is used for their business purposes. In this case, it will be treated as

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private asset. However, this option will not be available to individuals who have opted for the lump-sum tax regime or who claim expenses as a percentage of income. The term 'registered asset' will therefore have a much broader content and will affect a very wide range of taxpayers. For example, in the case of the lease of real property and its subsequent sale, the relevant income from the sale of the registered asset will be taxed as the individual's income from self-employment.

The Ministry of Finance has already declared that such a radical change was not the aim of the amendment. Let us therefore wait to see what the amendment will look like after comments are settled.

Prohibition on depreciation of foreign real property generating income exempt from taxation in the Czech Republic

A Czech tax resident will not be considered to have a registered asset if income flowing from this asset is only income from foreign sources for which the exclusion method is applied to avoid double taxation. If the taxpayer, a Czech tax resident, owns real property in the UK and rents it out (lease income is taxed in the UK and exempted from taxation in the Czech Republic under the Czech-British double taxation treaty), it will not be possible to depreciate the real property in the Czech Republic. By not being able to claim depreciation expenses, the effective tax rate at which post-exclusion income will be taxed will increase significantly. The tax position of these taxpayers will thus effectively worsen compared to others (e.g., those who apply the foreign tax credit method under the relevant double taxation treaty).

Bookkeeping

The current Accounting Act prescribes the obligation to keep accounting records for a selected group of individuals (e.g., an individual who is an entrepreneur registered in the Commercial Register or whose turnover exceeds CZK 25 million). The new draft Accounting Act establishes bookkeeping for individuals on a voluntary basis. However, the amendment to the Income Tax Act does not follow this approach and treats individuals keeping accounts as if they were not accounting entities. Such persons will not be able to derive their tax base from the results of their operations as has been the case so far, but their tax base will be determined in a similar way to other individuals (natural persons), i.e., on a cash basis.

However, the paradox is that many provisions of the amendment directly refer to the Accounting Act and introduce the valuation of things, services and debt according to the Accounting Act into the cash basis for determining the tax base. Although individuals will determine the tax base on a cash basis, a detailed knowledge of accounting will still be necessary to determine it correctly, which will undoubtedly be administratively demanding for them and cause disproportionate additional costs.

Transitional provisions

The transition to the cash basis for determining the tax base on the proposed effective date of the amendment, i.e., **1 January 2025**, will be regulated for all individuals who keep accounts by applying the provisions governing the transition from keeping accounts to keeping tax records as applicable on 31 December 2024. Taxpayers with rental income or income from self-employment switching from keeping accounts to keeping tax records will follow a similar procedure. Another option will be to use the transition from keeping accounts to claiming expenses as a percentage of income or using the lump-sum tax regime.

Cancellation of the period for which the tax return is filed

Since the taxable period for corporate income tax will be newly linked to the accounting (reporting) period, the Ministry of Finance proposes to delete the term 'period for which the tax return is filed' throughout the

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amendment. However, the submitter of the amendment has obviously forgotten that occasionally, individuals also file tax returns for a period shorter than the taxable period (i.e., the calendar year), e.g., in the case of death of a taxpayer.

Conclusion

Perhaps now is the time for the Ministry of Finance to consider setting aside personal income tax into a separate law. This amendment shows that the principles of corporate taxation (accrual principle) and the direct link to the Accounting Act cannot be applied across the board to individuals where the cornerstones of taxation are based on the cash principle.

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Tips and tricks

Principles of tax administration: material truth

Honesty gets you the furthest, and lies don’t travel far. With a bit of exaggeration, it could seem that these sayings were an inspiration for the Tax Procedure Code, as it enshrines the principle of material truth. In this article, we explain what this principle means, how it is applied, and how the courts view it.



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The essence of the principle

The principle of material truth means that the tax administration must base its decision on the actual content of a legal act or other relevant facts. In other words, the tax authorities must not be only interested in how something is formally recorded on paper but also in what actually happened.

The application of the principle

In practice, the principle of material truth is most often applicable when an entity tries to hide the true substance of a transaction to reduce its tax liability or avoid it altogether. The task of the tax authorities is therefore to establish the true state of affairs and to support their conclusions with concrete evidence.

Example from court practice

For example, the Supreme Administrative Court has recently dealt with several cases of disguised association activity where taxpayers provided their members with internet access in exchange for membership fees. Under the guise of association activities, they obtained tax benefits intended only for associations, i.e., the exemption from income tax of membership fees and the exemption from value added tax of the provision of services in return for membership fees. The tax administrator carried out extensive procedures to provide evidence in each case, which contributed substantially to proving simulated conduct - association activity. The tax administrator discovered, e.g., that these 'associations' had dramatically increased their profits even though they were primarily intended to carry out non-profit activities. Witness testimonies confirmed that the vast majority of memberships had the sole purpose of obtaining a favourable internet connection. Even the consequences of non-payment of membership fees were indicative of a wholly commercial approach, as members were immediately cut off from the internet or contacted to prevent them from leaving for a competitor. Based on the extensive evidence provided by the tax authorities, the Supreme Administrative Court confirmed that the "associations" only pretended to carry out association activities but in reality provided services for consideration. The application of tax benefits intended only for associations was therefore excluded in the cases under examination.

Implications

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For the purposes of tax proceedings, it is the actual substance of the conduct that is decisive, not its formal recording. However, it is the tax administrator who must not only reveal what actually happened but also explain how they came to these conclusions, and provide the evidence on which their decision was based. Therefore, we recommend that all steps be properly supported with evidence and justified in case the tax authority has doubts as to whether there is any disguised activity.

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Amendment to allow employees to self-schedule their working hours

The Ministry of Labour has set for itself the commendable goal to make labour-law regulation more flexible. To this end, it drafted several amendments to the Labour Code. One of the most significant changes to have already passed the legislative process is the possibility for employees to self-schedule their working hours.



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Currently, the Labour Code allows employers to delegate the right to schedule working hours to their employees only in the context of remote work (teleworking) and a shared workplace (where employees who share one job position may themselves divide the hours between them). Other employees may influence their working schedules only under an arrangement on flexible working time but nonetheless must work within the limits set by the employer in the form of fixed working time periods. This is now about to change: from **1 January 2025**, the amendment to the Labour Code will allow for the possibility to arrange that employees may self-schedule their working hours and shifts, subject to agreed-upon conditions.

The amendment does not specify these conditions. The explanatory memorandum to the bill states that the employer should (contractually) agree with the employee on the employee's obligation to observe statutory breaks, minimum rest periods, safety breaks, or maximum shift lengths. Employers will remain liable for any breaches. Other restrictions may also be recommended, e.g., that the employee should not schedule work for nights, weekends, or holidays. The agreement may also specify whether the working time should be evenly distributed or not.

Once employees are allowed to self-schedule their working hours, employers will still be obliged to keep records of working time. Therefore, it may be advisable to contractually agree on the employee's obligation to cooperate, e.g., by delivering timesheets at an agreed-upon frequency. It may also be practical to stipulate that under certain conditions, the employer may limit the employee's freedom to self-schedule their working hours.

The amendment explicitly provides that the Labour Code's regulations concerning working hours shall not apply to self-scheduling, except for the employee's obligation to be at their workplace at the beginning of the shift and to leave it only after the end of the shift, and the obligation to ensure that one single shift shall not exceed 12 hours. The employee's average weekly working hours agreed upon in their employment contract will have to be completed within a settlement/balancing period determined by the employer.

The amendment also deals with possible obstacles to work, vacations, and business trips: in these cases, a back-up working time schedule shall apply, which the employer will be obliged to set in advance. However, for other important personal obstacles at work on the part of the employee, employees who schedule their own working hours will not be entitled to wage or salary compensation (with exceptions).

As for the termination of the agreement on self-scheduling of working hours, the amendment assumes either that both parties will agree, or that one party will give notice with a 15-day notice period starting on the day the notice

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is delivered to the other party.

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Stricter sanctions to fight illegal work

Illegal work has recently come under the scrutiny of state inspection authorities and remains a central focus of their concern. For this reason, the Ministry of Labour and Social Affairs (MLSA) has proposed a further tightening of the rules concerning the 'Svarc system' (where dependent work is formally carried out by independent contractors). The bill is currently being discussed by the chamber of deputies and is scheduled to enter into effect on 1 January 2025.



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One of the basic changes the bill will introduce is a penalty of the **publication of the decision on the offence**. This form of punishment could be imposed on perpetrators of both illegal work and disguised agency employment. The decision on their offence will be posted on the official noticeboard of the State Labour Inspectorate for one year. The MLSA justifies this move by assuming that potential contractors will refuse to cooperate with persons who have committed such serious offences.

Changes are also being made to **the way in which inspections are carried out**: inspectors will be entitled to make audio and visual recordings during inspections and their preparatory work, even without the knowledge of the persons being inspected. This means that inspectors will not have to obtain the consent of the persons concerned, nor will they be obliged to announce their presence when taking urgent steps prior to the inspection itself. Although this new authorisation applies to all offences, the MLSA expects the new rules to mainly help inspectors when carrying out inspections of illegal work. The reason is that especially such inspections are often thwarted because of the duty to advise that recordings are being made. However, the inspection authorities will be obliged to use this approach solely where their purpose cannot be achieved in any other way.

The law will in some cases also allow for a more lenient approach. Under the new rules, individual inspectorates will have the authority not to initiate proceedings for offences with a low degree of social harm. It will be solely within the inspection authorities' administrative discretion whether they initiate the proceedings or defer the matter. They shall base their decisions on the circumstances of the offence, the way the offence was committed, and its consequences. This change will apply to offences under the Employment Act (e.g., illegal work) and to offences under the Labour Inspection Act.

Furthermore, supply recipients will no longer have to worry about being liable for the payment of a penalty if their supplier has committed disguised agency work. Under rules in effect since January this year, the Labour Inspectorate can demand they pay the penalty if it cannot be recovered from the offending contractor. However, due to a legislative error, the application of the concept is very complex and therefore in the future, the liability for the payment of the penalty will only arise where the contractor has allowed for the illegal work of a foreigner.

The amendment will make it even easier for the state to combat illegal work. It can be assumed that the legislation will continue to develop and that the penalties for illegal work will only become stricter.

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Czech Republic no longer recognises Russian non-biometric passports

Due to the current geopolitical situation, the Czech Republic has decided not to recognise Russian travel documents that do not have biometric elements, effective from 3 July 2024. The purpose of the measure is mainly to increase security and facilitate the identification of Russian citizens. The changes affect not only Russian citizens planning to travel to the Czech Republic but also those already residing in the Czech Republic.



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Czech authorities abroad have stopped accepting applications from holders of Russian non-biometric passports. At the same time, if a holder of a non-biometric passport submitted their application before the entry into force of this notice, the Czech authorities will not place a visa in this passport even if a positive decision on the visa application was made. All Russian citizens are now obliged to present a biometric document before a visa can be granted.

If a Russian citizen is staying in the Czech Republic based on a residence permit and holds a non-biometric passport, it is their obligation to apply for a new document. Since the embassies of the Russian Federation work in a restricted regime, a transitional period has been set until **15 September** for them to comply with this obligation. However, at present, it can take up to six months for a new document to be issued. Once a new passport is issued, the Ministry of the Interior of the Czech Republic must be notified of this within three working days.

Russian citizens residing in the Czech Republic after **15 September** may be fined if they do not have a valid biometric passport. However, if they hold a valid long-term residence permit, they shall still be regarded as residing in the Czech Republic legally. For pending applications, e.g., for an extension of the residence permit, a biometric document will have to be presented. For this, the administrative authority shall issue a call to remedy deficiencies in the application with a sufficient deadline. If the foreigner fails to comply with the set out requirements on time, the application will not be granted and the proceedings will be discontinued. However, even if the proceedings are concluded before the end of the transitional period, the obligation to have a biometric passport will remain.

Children under 15 years of age, persons enrolled in the Civil Society programme, and holders of visas and residence permits granted in the interest of the Czech Republic are **exempt** from the obligation to hold biometric passports.

The new rule will make it much more difficult for holders of Russian non-biometric passports to travel. The Czech Republic is not the only country that has stopped accepting such travel documents, thus it is necessary to keep

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abreast of the rules of entry for Russian citizens to their destination countries. If a holder of a Russian non-biometric passport plans to enter the Czech Republic after 15 September and does not fall under one of the exceptions, they may be refused entry. To persons affected by these new rules, we recommend applying for a new biometric travel document as soon as possible.

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Easier recovery of debts through payment orders

On 1 July 2024, the Act on Collective Civil Proceedings came into force, enacting the process of collective enforcement of consumer rights in the Czech Republic. However, together with the act, legislators passed completely unrelated amendments that partly change the regulation of payment orders and delivery service to persons who have no permanent residence and are therefore registered at competent authorities. Although these changes are subtle, they will have a significant practical impact.



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The basic elements of the law on class actions are summarised here.

A fundamental change is that **both payment orders and electronic payment orders (EPR in Czech) can now also be delivered by fiction via a data mailbox**. Up until now, if a defendant failed to log in to their data box, the court would cancel the payment order. Under the new rules, the payment order will now be deemed as having been served on the tenth day after the delivery of the data message. This also applies to natural persons who have voluntarily set up a data box and self-employed persons whose data boxes were set up automatically. If someone does not regularly collect their messages from their data boxes, they may fall prey to the pitfalls of payment orders. Should defendants fail to file a protest in time, their payment order will have the effect of a final judgment, while further procedural defence against such a decision is essentially minimised.

The limit on the amount of the EPR to a maximum of CZK 1 million has also been abolished. **Now, an EPR can be filed for any amount (i.e., even exceeding CZK 1 million), just like a standard payment order.** The EPR has stricter legal regulation in some respect: e.g., the court will reject it entirely if it does not contain all prescribed essential elements. On the other hand, it offers the claimant a reduction in costs in the form of **a court fee lower by 1% of the total amount claimed**.

The amendment also facilitates the service of court decisions to persons without a permanent residence but with a registration address at the competent authority. In the past, it was not possible to use this address for delivery service, and the person always had to provide an address where documents could be sent, which often resulted in documents being returned as undeliverable. Under the new rules, the courts may use the address of the registering authority. That authority will then post a notice on the official notice board asking the addressee to collect the document or request that it be sent to another address. If the addressee does not respond to the notice within 10 days of its publication, the document shall be deemed to have been served even if the addressee was not aware about the delivered document. However, neither the first documents to be served in proceedings nor documents for which substituted service is excluded may be served at the registering authority. The change will therefore not facilitate the service of payment orders. Nevertheless, it may bring more flexibility to ordinary court proceedings.

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Demerger by separation: new type of business conversion for more efficient restructurings

A major amendment to the Act on Conversions of Commercial Companies and Cooperatives (the Company Conversion Act) effective from 19 July 2024 has introduced a new type of conversion: the demerger by separation. This extends the range of companies' options as to the form of a demerger for both domestic and cross-border conversions. This change can make intra-group restructurings and other M&A projects faster, easier, and cheaper.



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Until recently, the Company Conversion Act distinguished only two forms of demergers:

- **a split-up**, where all assets and liabilities of one company (the company being demerged) are transferred to at least two successor companies, and the demerged company ceases to exist
- **a spin-off**, where the company being demerged does not cease to exist, but a part of its assets remains in the demerged company and another part of the assets passes to at least one successor company.

In both these forms, the shareholders/members of the demerged company become the shareholders/members of the successor company.

In the new form of demerger – **a separation** – the company being demerged does not cease to exist, but (unlike in a spin-off) the company itself (not its shareholders) becomes the shareholder of the successor company. It is in fact a specific type of contribution into another company.

The amendment introduces two types of separation, while their combination is also possible.

A separation with the formation of a new company/companies is essentially a new way of establishing a subsidiary. The newly established company (into which the assets and liabilities are separated) will be fully controlled by the company being demerged, which will become its sole shareholder.

- Before the amendment, to achieve such a structure, it was customary to establish a subsidiary company and then transfer the required part of the parent company's assets and liabilities to such empty company (in the form of a transfer of a part of a business or its contribution into the new subsidiary), or to carry out an asset deal (a transfer of individual specific items into the newly established subsidiary). Alternatively, it was possible to set up a new subsidiary and carry out a spin-off with acquisition, whereby the spun-off part of

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the assets and liabilities was transferred from the parent company to the new company. This option, however, encountered the limitations of the de facto impossibility of setting the decisive date of the conversion retroactively before the date of formation of the new company.

- Compared to the previous options, the process of demerger by separation is **simpler** (no need for a separate step of establishing a new company) and **clearer**. The newly created company will have the status of a legal successor of the company being demerged with respect to the part of the assets and liabilities being transferred to it within the separation. The rights and obligations (including any rights and obligations arising from labour relations) and contractual relations will also pass on to the new company, and creditors will not be able to plead the transaction's ineffectiveness. Further advantages for the entrepreneur arise in taxation.

In a separation with acquisition, a part of the assets and liabilities of the company being demerged is transferred to **an already existing company or companies**. The company being demerged then acquires a share/interest in that existing company, in the form of shares or units, in exchange for the separated part of its assets and liabilities. This opens a new possibility for structuring acquisitions or joint projects, as companies can contribute a part of their assets and liabilities into another company in exchange for shares in that company, possibly to be followed by a share deal.

Demergers by separation, can only be used for conversions of commercial companies, not cooperatives.

In previous articles, we summarised other legal and tax aspects of company conversions brought about by the legislative amendment.

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AI Act enters into force! Are you prepared?

On 2 August 2024, Regulation (EU) 2024/1689 of the European Parliament and of the Council laying down harmonised rules on artificial intelligence (AI Act) entered into force. The AI Act provides rules for the safe, responsible, and transparent use of artificial intelligence (AI) in the EU. Over the next two years, companies using AI will have to prepare for numerous new obligations.



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The AI Act impacts a wide range of entities, from AI system manufacturers to end users. If your company develops AI systems or uses off-the-shelf (ready-made) AI solutions in its operations, you should pay close attention to the regulation. First, companies will need to ask themselves whether their solutions meet the definition of an AI system under the AI Act. If yes, the next step will be to assess what level of risk the use of a particular AI system poses. The regulation classifies AI systems according to their risk level, and, generally, the higher the risk an AI system poses, the more obligations will fall upon the particular entity.

1. The first category comprises AI systems whose use poses **an unacceptable risk**. Their use and supply in the EU will be prohibited altogether. This category includes, e.g., AI systems for social scoring, systems designed to manipulate or biometrically categorise people based on age, gender, or race, and other similar systems that are contrary to EU core values.
2. The main objective of the new regulation is to cover the category of **high-risk systems**. This may include AI systems used in critical infrastructure (transport industry, energy sector), access to essential services (healthcare, banking, insurance, welfare), education, employment or law enforcement, or other systems identified according to a comprehensive key contained in the AI Act. The use of these AI systems could threaten fundamental rights, freedoms, and security, and therefore this category is subject to the strictest regulation and a wide range of obligations for the entities concerned.
3. AI systems where **the risk lies in a lack of transparency** will be subject to numerous information obligations to ensure that the subject who is exposed to an AI interaction (e.g. chatbot, deepfake content, etc.) is informed of this fact and is thus free to decide whether to continue or stop the interaction.
4. In addition to the above categories, the AI Act also regulates **general-purpose AI models and general-purpose AI models with systemic risk.** This special category was included in the AI Act in response to the advent of ChatGPT and similar large language models.

It is high time for companies that want to supply AI systems to the European market or deploy them in their operations to start preparing for the new regulation. Within six months, i.e., by **2 February 2025**, they must identify and prevent the use of banned AI systems. Failure to comply with this ban carries **strict penalties** of up to EUR 35 million or 7% of their global annual turnover. From **2 August 2025**, obligations for general-purpose AI models will enter into effect. The widest range of obligations impacting high-risk systems will enter into effect in stages, on **2 August 2026 and 2 August 2027**.

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Revolution in data management? New law promises breakthrough in access to public administration data

Will it be data and not the citizens that will circulate between authorities, as the government promised in its manifesto? In April, the Digital and Information Agency published a draft of a new law on data management and controlled access to data. Its aim is to make the transfer of data between the public administration and the private sector more efficient.



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The public administration has at its disposal a huge amount of data with significant information potential, but it remains unused. Currently, data cannot be accessed by external parties such as scientists, researchers, or journalists, and can often not even be shared between individual authorities. Moreover, the authorities themselves often do not know what data they have. This should now change.

The new bill aims to address the long-term problems associated with inappropriate data handling practices and set legislative rules for access to the data. It proposes to introduce **controlled access**, which will enable repeated access to data or their derivatives for statutory purposes in the public interest, and at the same time provide security against infringement on protected rights (e.g. as regards data containing personal data, trade secrets, or intellectual property of third parties).

Obliged entities will now have **a general obligation** to properly manage, maintain the sovereignty of, describe, and keep a catalogue of data. Entities may request controlled access to data for scientific research, the exercise of the right to freedom of expression and the right to information, ensuring the transparency and supervision of public administration, or for teaching and educational purposes. Requests for controlled access to data will be assessed by the Digital and Information Agency.

If the law is adopted, it should be possible to find out what data a particular authority has and obtain access to that data.

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CBAM: end of default values

In its Implementing Regulation of August 2023, the European Commission in certain cases allowed the reporting of emissions for the purpose of filing Carbon Border Adjustment Mechanism (CBAM) reports based on calculations using published default values. However, 31 July 2024 is the last day when reporting entities may use the default values for the calculation of their direct and indirect emissions.



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The substantive condition for the possibility to use default values was the unavailability of data on the part of producers or suppliers. As regards the next CBAM reports for the third and fourth quarters of this year, however, default values will no longer be available for use - with an exception - and the actual values according to the EU methodology will have to be reported.

The default values greatly simplified the calculation of direct and indirect emissions contained in goods imported from third countries that fall into selected categories subject to CBAM. For complex goods, **from 31 July** until the end of the transition period, it will be possible to use default values for a maximum of 20% of the calculation of the total emissions involved. Complex goods are defined as goods whose production requires both direct inputs (typically materials - direct emissions) and indirect inputs (typically electricity consumption - indirect emissions). Where partial data on emissions relating to such goods will be unavailable, it will be possible to estimate a 20% portion of such emissions. However, no estimates can be used for simple goods whose production involves only direct inputs.

From our practice we see that the implementation processes for CBAM, or ESG policy, have not been fully completed, especially in large corporations. Obtaining data on imported goods from producers and suppliers is very problematic and, in some cases, even impossible. At the same time, changes to existing long-term contracts for the purchase of goods and the negotiation of new ones impose significant administrative costs on companies. In many cases, entities subject to the CBAM reporting may even lose their market position. From the sources available to us, we do not yet see any effort by the European Commission to extend the possibility to use default values.

If you are concerned about CBAM and need to set up internal mechanisms or calculate emissions, please do not hesitate to contact us.

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Subsidies to digitise your business

On 15 July 2024, the Ministry of Industry and Trade opened a call for applications under the Operational Programme Technology and Applications for Competitiveness called Digital Enterprise - Digital Enterprise - Call I.



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Applications for support will be accepted until 31 March 2025. The call is open to small and medium-sized enterprises. Total funds for allocation are CZK 1 billion. **The main supported activities include**:

- digital transformation of an enterprise
- logistics and warehouse technologies and other non-production technologies intra-company connectivity (including sensor networks)
- cybersecurity
- creating a digital twin
- BIM and CDE systems
- selected IT training courses.

The project must meet at least one of the following **conditions for an initial investment**:

- a fundamental change in the overall production process
- setting up a new establishment
- expansion of the capacity of the existing
- establishment
- expansion of the production range.

Support can be obtained for expenses incurred for tangible and intangible fixed assets, services and other expenses. Eligible expenses are specified in Annex 3 of the call. On the other hand, expenses for the acquisition of tangible assets used for an applicant's core business are not eligible. Eligible project expenses must be at least **CZK 2.5 million** and not more than **CZK 50 million**. The aid intensity varies from 25% to 60% of eligible expenses, depending on the region in which the project is carried out and whether the applicant is a small or medium-sized enterprise.

An applicant may submit only one application for support but may carry out the project in up to ten different locations. Implementation is possible throughout the Czech Republic, excluding Prague. The project must be completed by **31 December 2026** at the latest.

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Subsidies

Transport 2021-2027: Hundreds of millions for charging and hydrogen stations

At the end of July, the Ministry of Transport updated the schedule of calls under the Operational Programme Transport 2021–2027. This programme continues to support key transport projects focusing on the expansion of infrastructure for alternative fuels for passenger and freight vehicles, and the digitisation and development of rail transport.



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The Transport 2021–2027 programme is a support instrument for financing transport projects aimed at efficient, accessible, and environmentally friendly transport. The priority for the Czech Republic is the development of a backbone, suburban, and urban transport infrastructure and sustainable transport, which will improve regional connectivity and links to other EU countrieXXWs. The main calls announced focus on supporting infrastructure for alternative fuels, such as the construction of charging stations with battery storage, fast charging stations, conventional charging stations, and hydrogen filling stations. The selected calls with information on their timing and funds for allocation are summarised below:

Name	Funds for allocation	Call announced in	Acceptance of applications ending in
Support for the development of fast charging infrastructure for trucks	CZK 1 000 mil	12/2024	04/2025
Support for the development of charging infrastructure with battery storage	CZK 300 mil	01/2025	05/2025
Support for the development of fast charging infrastructure for passenger vehicles	CZK 1 385 mil	09/2024	01/2025
Support for the development of conventional charging stations in cities and municipalities	CZK 370 mil	10/2024	02/2025
Support for the development of hydrogen filling stations along the main TEN-T network*	CZK 180 mil	11/2024	03/2025
Support for the development of hydrogen filling stations in urban nodes	CZK 240 mil	11/2024	03/2025

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For all the calls, applications can be submitted by the owners or managers of the involved infrastructure in the Czech Republic.

The maximum aid intensity can be up to **85%** of eligible expenses. Applications for support will be assessed in terms of the project's cost-effectiveness, preparedness and relevance.

The Ministry of Transport also announced its plans for calls focused on rail transport. More detailed information can be found here.

** TEN-T - Trans-European Transport Network is a network of road and rail corridors, international airports, and waterways in the European Union.*

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Case law

Statutory representatives liable for a corporation's tax arrears?

In a recent judgment (10 Afs 4/2024-38 of 18 June 2024), the Supreme Administrative Court (SAC) dealt with a case in which the tax authority turned to the statutory representative of a corporation on the grounds of his liability. Although the Tax Procedure Code has provided this option for many years, the financial administration has not used this concept so far. The SAC has now confirmed this procedure for the first time and formulated the basic rules for its application.



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Subject-matter of the case

Together with other persons, a company's statutory representative had been convicted of the crime of tax evasion committed by extracting undue advantages from the company in which he performed his office. The company was subsequently dissolved with liquidation, and the tax authority was unable to satisfy its tax claim. It therefore turned to the statutory representative and demanded payment of the tax based on his liability pursuant to the Tax Procedure Code.

Liability for statute-barred claims

The court first confirmed that the statutory representative as a guarantor may indeed be obliged to pay the company's tax debts under the Tax Procedure Code. However, the Supreme Administrative Court rejected the procedure of the tax authorities which assumed that liability for unpaid tax could be invoked even if a company's claim for damages against its statutory representative had already been statute-barred.

A statutory representative's liability for unpaid tax must always be backed up by the law. If the statutory representative's liability under such a law (in this case the Civil Code) has already been statute-barred, no liability may arise under the Tax Procedure Code. However, the statutory representative must always explicitly plead the limitation of their liability. The court also pointed out that in exceptional cases, pleading the limitation may be an abuse of law or contrary to good morals. In such cases, the tax authority could very well proceed to recover even a statute-barred claim against the statutory representative.

Liability for claims with the lapse period expired

For liability to arise, it is not necessary to have committed a criminal offence; any breach of managerial duties, in particular a breach of due care, suffices. If a statutory representative causes the company to incur a tax debt by the

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above, they will not be able to avoid their obligation to pay the debt even if the company is dissolved. Where the extraction of an undue tax advantage is also a criminal offence, liability arises even if the tax assessment period has expired. In such a situation, the tax can be assessed until the end of the second year following the final conviction. The expiry of the basic period for tax assessment is then disregarded, and it is possible to exceed even the maximum period of 10 years.

Final recommendations

Statutory representatives cannot be relieved of their liability by delegating some of their duties to third parties, such as entrusting an accounting firm with bookkeeping, as here too, it will be examined whether the statutory representatives chose the firm with due care and whether any deficiencies in the accounting could have been prevented.

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Case law

SAC on tax treatment of sale of unfinished real estate and related project

The Supreme Administrative Court (SAC) dealt with the tax deductibility of costs related to a development project upon the sale of unfinished real property. The tax administrator did not recognise most of the costs as tax relevant, and the Supreme Administrative Court confirmed this.



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A development company purchased land with real property to implement a new development project. In this context, the developer incurred costs for the implementation of the project, which included demolition work, legal services, interest on loans, and, last but not least, penalty costs.

Also involved in the project was an affiliated company, which was to obtain an architectural study, documentation for the zoning permit, and other related requirements, through a subcontractor. The rights arising from the pending proceedings and from the project were to be transferred to the developer only once the zoning permit was issued, which happened in 2016.

Sale prior to the issuance of a zoning permit

However, in 2015 the developer decided to sell the formally prepared project to an external investor. In its corporate income tax return, they claimed as tax-deductible all expenses related to the disposal of the project, including amounts related to its preparation that was to be supplied by the related party.

The tax administrator did not accept most of the claimed expenses due to their insufficient link to the generated income in terms of substance and timing. Within the proceedings, the tax administrator did not dispute the individual types of the costs but focused on the substance of the transaction and the related contractual documentation.

In the tax administrator's opinion, which was subsequently confirmed by the Supreme Administrative Court (SAC), in 2015 the developer in fact sold only the land and real property, not the development project with the issued zoning permit as a whole, as at the time of the sale, the developer was not yet the owner of the rights to build the project; these were only acquired in 2016. Therefore, since the developer did not own all rights to the project in 2015, they could not, according to the tax administrator, have sold the project in that year and included the related costs of the project in the tax-deductible expenses for that period. Only the costs directly related to the disposal of the land and related real property were recognised by the tax administrator as tax-deductible expenses in 2015.

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Principle of substantive and temporal link

In the implementation of development projects, multiple entities with different rights and duties may be involved throughout the process. A thorough analysis of the specific situation is therefore always necessary. In the present case, no precedent was established seeking to define tax-deductible expenses upon the transfer of an unfinished project; the judgement has merely highlighted the importance of the principle of substantive and temporal link.

Although the judgment does not further elaborate on the structure of costs of acquisition of assets, it would certainly be interesting to see how the court would deal with the inclusion and subsequent tax deductibility of penalty costs, which in the present case constituted the most significant portion of the claimed expenses.

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Case law

CJEU: supplies provided within VAT group not subject to tax

In case C 184/23 Finanzamt T, the CJEU dealt with a dispute between the German tax administration and a foundation governed by public law. In the same case, judgment C 269/20 had already been delivered, which dealt with a VAT group and the supplies made within that group. The case has then returned to the CJEU with further preliminary questions.



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Foundation S was the controlling entity of company U and of a university operating a teaching hospital. Company U provided cleaning, sanitation, and other services to foundation S for the entire building complex that foundation S managed. Foundation S carried out its own economic activity in this building compound, but also used a part of the complex for education – in this case acting as a public authority and not regarded a taxable person.

The German court again returned to the CJEU with questions as to **whether supplies made between persons forming a VAT group must be subject to VAT,** and whether **the supply recipient not being entitled to deduct input tax** should be considered in this context.

The CJEU held that the supply of a service is taxable only if there is a legal relationship between the supplier and the supply recipient under which supplies are exchanged. This means cases where the provided consideration represents the actual counter-value for the supply made by the supplier to the recipient. To determine whether such a legal relationship exists, it must be ascertained whether the provider of the supply carries out an economic activity independently.

Furthermore, the CJEU held that once a person becomes part of a VAT group, the EU VAT Directive precludes them from being regarded as a taxable person on a separate basis, whether in relation to other persons or to persons within in the group, and from filing a separate VAT return. Only one person is entitled to file a VAT return for the VAT group. It follows from this assumption that **when a service is supplied by a member of a VAT group to another person within that group, there is no need to examine the condition of independence** - such a supply will always be outside the scope of VAT.

The CJEU also reiterated that a **VAT group acts as a single taxable person for VAT purposes, i.e., it is not the individual members who are entitled to the deduction but the group as a whole**. The fact that the recipient of the supply was not entitled to the deduction therefore has no bearing on whether supplies made between members of the group are subject to output VAT.

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Thus, the CJEU merely confirmed that supplies provided within the VAT group do not fall within the scope of tax, and the fact that the recipient of the supply could not benefit from the right to deduct does not alter this conclusion.

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Case law

CJEU on rejecting application for VAT refund

The Court of Justice of the European Union (CJEU) has held that the one-month time limit for submitting additional information in the proceedings for a VAT refund is not a limitation period. If national legislation does not allow new evidence to be submitted in the appeal process, it systematically prevents the refund of VAT.



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A Slovak company operating in the energy sector carried out assembly and installation work in Hungary. For this purpose, the company purchased various supplies in Hungary, in respect of which they subsequently applied for a VAT refund. The Hungarian tax authorities called upon the company to provide additional information on the matter within a deadline of one month. The company did not respond, and the tax authority discontinued the proceedings. The company then appealed and provided all the requested information. The appellate authority upheld the decision to reject the application on the grounds that new evidence could not be submitted in the appeal if the appellant had already been aware of such evidence before the first decision was issued.

The company brought an action against this decision before the Budapest municipal court. In particular, the company argued that the prohibition of the submission of new evidence under Hungarian law constituted a substantive limitation of the right to appeal, and that the one-month period to remedy the deficiencies under the directive was not a limitation (expiry) period.

Following the submission of preliminary questions by Hungary, the CJEU first pointed out that according to **the principle of neutrality**, input VAT must be refunded if the substantive requirements have been met, even if the taxable person has not complied with certain formal requirements. The opposite approach may only be applied if the failure to comply with the formal requirements results in the impossibility to produce reliable evidence of compliance with substantive requirements.

According to the CJEU, the facts of the case under examination imply that the dispute in the original proceedings was not about a breach of formal requirements resulting in the impossibility to produce evidence of compliance with the substantive requirements, but about the date by which such evidence must be produced.

The CJEU also referred to its decision in Case C 133/18 Sea Chefs Cruise Services, according to which the one-month period provided for in the directive is not a limitation period. According to the principle of good administration, the tax administrator should ensure that when carrying out their inspection duties, they conduct a diligent and impartial examination of all relevant aspects to make sure that they have the most complete and reliable information possible when making their decision. In the present case, therefore, the national legislation constitutes a substantive **limitation of the right of appeal**.

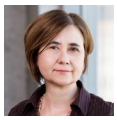
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According to the CJEU, if an application for a VAT refund is rejected, the applicant who failed to provide additional information within the one-month period has the right to appeal against the rejection. Within the appeal, they have the possibility to remedy the deficiencies of their application by submitting additional information. If the tax authority could not take into account a late reply to a request for additional information, with the result that such late replies would be systematically rejected, this would necessarily lead the tax administrators to breach the principle of good administration, as they would be issuing a decision which they know may be based on incomplete or even incorrect information.

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News in brief, August 2024

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



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Domestic news

- The Ministry of Finance has published a summary report on the activities of the Financial Administration of the Czech Republic and the Customs Administration of the Czech Republic for 2023.

- The following was published in the Collection of Laws and International Treaties:
  - Notice of the Ministry of Foreign Affairs 206/2024 on the Treaty between the Czech Republic and the United Arab Emirates for the avoidance of double taxation in the field of income taxes and for the prevention of tax evasion and avoidance
  - Decree No. 218/2024 amending Decree No. 117/2012 Coll., on the detailed regulation of the activities of a pension company and a participation fund
  - Decree No. 219/2024 amending Decree No. 207/2021 Coll., on billing for supplies and related services in the energy sectors
  - Decree No. 222/2024 amending Decree No. 264/2020 Coll., on the energy performance of buildings
  - Amendment to the Labour Code (230/2024) in effect from 1 August 2024.

- Following the completion of the comment procedure, the Ministry of Finance has published a bill amending Act No. 563/1991 Coll., on Accounting; Act No. 93/2009 Coll., on Auditors; and Act No. 416/2023 Coll., on Top-Up Taxes for Large Multinational Groups and Large Domestic Groups:
  - The draft amendment to the Accounting Act and the draft amendment to the Act on Auditors implement EU legislation and include an increase in the thresholds for total assets and for annual aggregate net turnover set as two of the criteria to categorise accounting entities according to their size. They also modify obligations concerning sustainability reports. The proposed effective date of both amendments has been postponed to 1 January 2026.
  - The draft amendment to the Act on Top-Up Taxes has been significantly supplemented following the comment procedure. One of the reasons for the supplementation is to ensure the qualified status of the Czech top-up tax. The bill will now be discussed by the government.

- In July, the government approved an update of the Czech Hydrogen Strategy, which is part of the reforms required by the European Commission under the National Recovery Plan. The government has declared hydrogen to be an important element of Czech energy policy as a replacement for fossil fuels in transport, a carrier for transport and energy storage, a raw material for the chemical industry, and a source of heat.

Foreign news

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- In its decision C-623/22 concerning the implementation of Council Directive 2018/822 (DAC 6) in Belgian legislation, the CJEU did not find any facts in the issues under consideration that could render the directive invalid (extension of the reporting obligation to certain indirect taxes, obligation to report arrangements that comply with the law). The court also held that although several key concepts introduced by DAC 6 are broad (e.g., the concept of cross-border arrangements), they are nevertheless "set out in a sufficiently clear and precise manner" and do not constitute a breach of the EU Charter of Fundamental Rights.

- The CJEU has also commented on its previous decision C-694/20 and clarified that the part of the directive requiring advisers to inform other advisers and the client of their confidentiality is only invalid in relation to attorneys. More information can be found here.

- The European Commission has published its Annual Report on Taxation. The report provides an overview of the set-up and performance of EU member states' tax systems.

- The OECD has launched a public consultation on the XML editor and user guide for the Global Information Return (GIR) under Pillar 2. This initiative is intended to facilitate the preparation and submission of the returns and provide a technical format for the exchange of GIR information between tax administrations.

- The OECD Working Party on the Pillar 1 Multilateral Convention has postponed the deadline for signing the agreement to a yet undetermined date (the last deadline was 30 June 2024). No revised timetable has been announced.

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