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In brief

October 2020

Editorial

Soon it will be a year since we came up with the Czech audio version of Tax and Legal Update – Audiodaňovky. The statistics show that the Audiodaňovky have become quite popular – every month, hundreds of you tune in to listen to a couple of minutes' worth of the most important news. If you have not yet come across the Czech audio version, you can find it on [SoundCloud](#), [Apple Podcasts](#), and [Spotify](#).

Around this time last year, we were busy preparing our biggest client event – the Tax and Legal Forum. This year, for obvious reasons, this will be more difficult than usual. During the first wave of the pandemic we had hoped that by autumn things would be back to normal and we would again be able to welcome you live to share knowledge and experience or just to talk. Since the current situation is rather unfavourable, it is likely that the biggest tax-legal conference in the Czech Republic will be completely online. In any case, we will keep you informed so that you won't miss out on the most important tax and legal news for 2021, whatever the form may be.



Ladislav Malůšek
Partner
KPMG Czech Republic

Changes to tax depreciation to support investment

Among other things, the government intends to reboot the economy with measures relating to corporate income tax, proposing a reduction of the tax depreciation periods for a selected group of tangible fixed assets, an increase of the limit for treating an investment/expense as a tangible fixed asset, and the abolishment of the category of intangible assets for income tax purposes. The introduction of these measures would mean a reduction in the tax liability for corporations and more funds for their investments.



Michaela Thelenová
mthelenova@kpmg.cz



Mirka Malá
mmala@kpmg.cz

The 2021 governmental tax package (Print 910), which also includes amending proposals regarding the depreciation of assets, is now to be discussed in the chamber of deputies within the second reading. These proposals have already been approved and recommended by the budget committee.

The reduction of depreciation periods is proposed as extraordinary depreciation, which we know from the financial crisis in 2009 and 2010. It would be possible to apply extraordinary depreciation charges to tangible fixed assets belonging to the first and second depreciation categories and acquired in the period from 1 January 2020 to 31 December 2021. Tangible assets in the first depreciation category would be depreciated without interruption over 12 months, on a straight-line basis, and up to 100% of the input cost. Tangible assets in the second category would be depreciated over a period of 24 months: the first 12 months on a straight-line basis up to 60% of the input cost and the subsequent 12 months on a straight-line basis up to 40% of the input cost. Depreciation charges would be set for months, not for years. The application of the extraordinary depreciation would be voluntary for taxpayers.

Another proposal suggests **increasing the limit for treating an investment/expense as a tangible fixed asset** and technical improvements thereof from the current CZK 40,000 to CZK 80,000. As a result, a larger number of acquired tangible assets could immediately be expensed, or their accounting depreciation could be claimed as deductible expenses for income tax purposes. The new threshold would have to be used for all tangible assets acquired and all technical improvements completed and put into regular use from the amendment's effective date. Voluntarily, the new threshold could also be applied to assets and technical improvements acquired/completed after 1 January 2020.

The last proposal, offering simplification rather than tax savings, is **the abolition of the category of intangible assets** and their tax depreciation in the Income Tax Act. Accounting depreciation charges would then be treated as deductible expenses. As with tangible assets, this new arrangement could also be applied voluntarily to intangible assets acquired after 1 January 2020. Expenses for research and development, software and intellectual property rights incurred after the amendment's effective date would no longer be considered intangible assets from an income tax perspective.

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Current state of subsidy programmes

The end of the Operational Programme Enterprise and Innovation for Competitiveness (OPEIC) period is approaching. Below, we provide an overview of the calls currently open, mainly focusing on research and development and innovations in production. At the same time, the Technology Agency of the Czech Republic (TA CR) has also announced new grant opportunities.



Karin Stříbrská
kpmg@kpmg.cz



Kateřina Balabánová
katerinabalabanova@kpmg.cz
+420 541 421 394

Calls to participate in OPEIC

OPEIC programmes currently open include **the Potential Programme**, which supports the establishment or the expansion of research and development centres. The programme aims to support investment expenditure on tangible and intangible assets, newly built constructions and other equipment, covering 50% of eligible expenses and distributing a subsidy per project ranging between CZK 2 million to CZK 50 million. Applications will be accepted until 23 November 2020.

The Application Programme helps cover operating expenses incurred to perform industrial research and experimental development projects. Depending on the programme conditions, support is provided in respect of 25–65% of eligible expenses such as wages, contractual research expenses, research and development advisory services, depreciation of tools, devices and equipment, additional overheads and other operating expenses. Large businesses carrying out projects but not cooperating with small or medium-size businesses may receive subsidies ranging between CZK 2 million to CZK 50 million; projects meeting the criteria of intervention codes 065 and/or 063 (see below) may receive subsidies ranging from CZK 2 million to CZK 100 million. Applications will be accepted until 15 December 2020.

The Innovation Programme is aimed at supporting innovative activities in production. Applications will be accepted from 15 October 2020 to 29 January 2021. The programme supports expenditure on constructions, technologies, software and data, project documentation, intellectual property rights, product certification, and marketing innovation. The aid intensity for large enterprises is 25% and the granted project subsidy may be in the range of CZK 1 million to CZK 75 million.

To participate in the above calls, large businesses must continue to fulfil intervention code criteria, in particular those of **intervention codes 065 and 063** (except for the above mentioned projects within the Application Programme), which mainly cover projects having a positive impact on the environment. They must therefore focus on the low-carbon economy and climate change resilience (code 065) or cooperate with an SME on a given project (code 063).

Calls announced by the Technology Agency of the Czech Republic (TA CR)

In September, TA CR informed that it was planning to announce the **fourth call under the TREND programme**

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supporting industrial research and experimental development on 13 January 2021. This will be a call to participate in Sub-Programme 2 – Newcomers, designed for businesses that have not been drawing research and development subsidies exceeding CZK 1 million for the last five years.

The TREND programme as a departmental programme of the Ministry of Industry and Trade mainly focuses on enhancing the international competitiveness of enterprises, expanding their markets abroad and penetrating new ones. Project outputs that will be supported include industrial design or utility models, prototypes or functional samples, software, pilot plants or verified technology, and patents or methodologies (both only in combination with previous results).

Support will be provided in respect of operating expenses (wages including scholarships, subcontracting, project-related indirect and direct costs), with a maximum aid intensity of up to 80% and a maximum subsidy per project of EUR 15 million. Support may also be drawn by applicants from Prague.

Within the evaluation process, projects concerning sectors such as Industry 4.0, Automotive, Technology 5G or projects aimed at mitigating health threats such as COVID-19 and their effects will be given preference. Furthermore, the programme favours projects carried out in structurally affected regions; these together with other detailed information will be specified in the tender documentation at the moment the call is announced.

Should you be interested, we will provide you with more detailed information on the programmes or assess the adequacy of the above programmes and other specific criteria for your planned activities.

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Reporting under DAC 6 postponed in the Czech Republic and other EU member states

The Czech Republic has utilised the option to postpone reporting duties arising from DAC 6 until the first months of 2021, as made possible by the COVID-19 DAC amendment adopted in response to the COVID-19 pandemic. Notably, some EU member states did not choose this option, or to a limited extent. As a result, reporting deadlines will differ across Europe.



Jana Fuksová
jfuksova@kpmg.cz



Matěj Kolář
kpmg@kpmg.cz

[As we already informed you](#), at the beginning of the summer the Czech Republic announced that it will opt to postpone the deadlines for the first-time reporting of cross-border arrangements. On 25 September this year, a government decree extending these deadlines entered into effect, stipulating the following:

- For cross-border arrangements whose first steps were taken between **25 June 2018 and 30 June 2020**, the reporting deadline has been extended to **1 March 2021**.
- For cross-border arrangements made available or ready for implementation or whose first steps were taken between **1 July 2020 and 31 December 2020**, the reporting deadline has been extended to **1 February 2021**.
- For cross-border arrangements with respect of which aid, assistance or advice was provided by an auxiliary intermediary before **31 December 2020**, the reporting deadline has been extended to **1 February 2021**.
- For updates of data in selected schemes concerning changes that occurred before **31 December 2020**, the reporting deadline has been extended to **30 April 2021**.

Note: when setting the deadlines for reporting cross-border arrangements, weekends are also taken into account.

While the reporting duty under Czech law has been postponed, please note that some EU member states including Germany, Austria, and Finland did not opt for a postponement.

Germany has not postponed any deadlines at all; hence new cross-border arrangements originated after 1 July 2020 still have to be reported within 30 days. Arrangements whose first steps were taken before this date had to be reported by 31 August 2020. Finland also decided to observe the originally planned deadlines. Austria has effectively extended the deadlines by three months: failure to meet the reporting duty will be penalised only after 1 November 2020.

Businesses and corporate groups operating in other states as well as in the Czech Republic thus have to keep abreast of the different deadlines for first-time reporting, as per national legislations.

Czech digital tax: when and in what form to expect it

A proposal for the introduction of a digital tax has been before the chamber of deputies for several months now. The originally proposed effectiveness from mid-2020 has come and gone. The introduction of this tax is currently being debated again.



Diana Marková
dmarkova@kpmg.cz



Matěj Kolář
kpmg@kpmg.cz

[In this article](#), we among other things already discussed the proposal to reduce the tax rate from 7% to 5%. After a deputy of one of the governing parties submitted this amending proposal, this change already seemed like a done deal in June. But even after a few months, the official proposal is still a rate of 7%. To reduce the rate by 2%, deputies would have to pass this amending proposal during the third reading. On the other hand, it must be acknowledged that during the summer, deputies did not have time to discuss a digital tax thanks to COVID-19 and the resulting limited operation of the chamber. The related second-reading discussions did not begin until the second half of September and were subsequently terminated due to a lack of time.

The effective date of this act itself is another question that cannot be answered at this time. The bill in its current version should become effective on the 15th day of its promulgation in the Collection of Laws and this was supposed to be mid-2020. One of the amending proposals filed by deputies of the governing parties suggests postponing effectiveness to 1 January 2021. To achieve this goal, the debate on the bill and related amending proposals in the chamber of deputies will have to conclude in the upcoming weeks.

Coordination Committee: When can the sale of real property be treated as losing rights to a business establishment from a VAT perspective?

The Czech Chamber of Tax Advisors submitted a paper for discussion to the Coordination Committee of the General Financial Directorate (GFD) and the Chamber of Tax Advisors dealing with when, from a VAT perspective, a transaction can be treated as a sale of real property and when a loss of rights to a business establishment.



Martin Krapinec
mkrapinec@kpmg.cz



Dominik Kovář
dkovar@kpmg.cz

Imagine the following situation: A seller decides to sell real property they have held for a long time, with its premises having been leased to several tenants. The buyer plans to continue to lease out the property; therefore, the seller will transfer the property including lease contracts, i.e. the buyer will replace the seller as the lessor in the existing contracts.

In assessing whether the above transaction involves just a sale of real property or also a loss of rights to a business establishment, the GFD drew attention to the existing case-law of the Court of Justice of the EU, according to which the loss of rights to a business establishment must be evaluated taking into consideration the nature of the seller's economic activity and the buyer's intentions. If a corporation is involved in real estate development activities, the sale of real property including tenants cannot be treated as losing rights to a business establishment: for developers, real property does not constitute a separate part of their business, but rather is an inventory item intended for sale.

According to the GFD, situations that can be considered as losing rights to a business establishment include, for example, when a corporation owning several items of real estate in the Czech Republic (as a real estate investor) transfers real property including lease contracts and these contracts do not cease to exist during the transfer. At the same time, the buyer obtains a suitable structure of assets sufficient to continue in the seller's original economic activity and does not terminate this activity after the acquisition.

To assess whether a transaction involves the loss of rights to a business establishment, it is also necessary to examine whether the transfer involves a set of components sufficient to enable the buyer to further perform the original economic activity. Without further consideration, the mere sale of real property including related lease contracts can thus not be treated as losing the rights to a business establishment for the purposes of the VAT Act.

If you are planning to sell real property in the near future, please do not hesitate to contact us. We will be happy to help you choose the most suitable option for you.

Czech Republic implements MLI into double taxation treaties

The Czech Republic has joined the states that have deposited their instruments of ratification for the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI, short for multilateral instrument) in Paris this year, thereby pledging to gradually implement the adopted principles into 52 double taxation treaties with states also having ratified the MLI.



Luděk Vacík
kpmg@kpmg.cz



Miloslav Zeman
miloslavzeman@kpmg.cz

The MLI is a collective instrument whose standards are subsequently implemented into double taxation treaties bilaterally concluded between the states that have decided to apply the MLI.

The Czech Republic only joined the convention to the extent of the minimum standard including the rule to prevent treaty abuse (principal purpose test, PPT) and the rule to allow for the effective resolution of disputes by mutual agreement (dispute resolution).

The adopted principles will gradually be implemented into the 52 double taxation treaties the Czech Republic has so far entered into. The Czech Ministry of Finance publishes amendments to relevant treaties in form of *communications on treaties* in its Financial Bulletin. To date, amendments associated with the implementation of the MLI into the double taxation treaties between the CR and Poland, Austria, Latvia, Serbia and Montenegro, Lithuania, Japan, Australia, Canada, Slovakia, Ireland, and Malta have been made public.

Impact of health ministry's protective measures on travel and employment in the CR

Since 5 October 2020, a new protective measure of the Ministry of Health has been in effect, aiming to slow down the spread of COVID-19 in the country. The measure restricts the crossing of borders by both Czech citizens and foreigners, and is closely linked to the ministry's continuously updated list of states, dividing them into low-risk, low-risk with PCR test required, and high-risk countries.



Romana Szutányi
kpmg@kpmg.cz



Katarzyna Bartkowiak
kpmg@kpmg.cz

The conditions for entering our territory and the rules to be observed for a certain period of time after entering the territory have been set depending on the country from which a person arrives in the Czech Republic.

Citizens of low-risk (green) countries can usually travel to the Czech Republic without restrictions, unless they stayed in a high-risk country for more than 12 hours in the last 14 days. Citizens of some low-risk countries where the epidemiological situation is worse are subject to certain restrictions if they plan to work in the Czech Republic.

Citizens of high-risk (red) states remain prohibited from entering Czech territory, with some exceptions. Exceptions apply, e.g., to holders of long-term residence permits in the Czech Republic, and in some cases, to family members or workers in international transport.

Highly important is the change in the rules for entering the Czech Republic from high-risk countries. All persons, including Czech citizens, who stayed for more than 12 hours in the last 14 days in these countries, must notify the relevant Regional Public Health Office of their arrival in advance, by completing an electronic arrival form. Proof of completion of this form must be provided, upon request, at the border/residence check and to bus/air travel service providers, if relevant. Arriving persons must also undergo a SARS-CoV-2 test within five days of entering and submit the results to the relevant Regional Public Health Office within seven days. In some cases, this can be substituted by a negative test not older than 72 hours carried out in another EU member state. At the same time, persons entering the Czech Republic from high-risk countries must limit their movements during the first 10 days and wear respiratory protective equipment throughout this time. This duty does not apply to Czech citizens and some foreigners – holders of long-term residence permits, provided that their travel was a part of a package tour to specified tourist destinations.

The measure also brings changes in the employment of some foreigners. Foreigners from high-risk countries and foreigners from low-risk countries with required PCR test who stayed there for more than 12 hours in the last 14 days shall also be subject to the above mentioned restriction of movement for 10 days. An exception is the travel to employment: workers may attend work even before the expiry of the 10-day period, on the condition that they present to the employer a negative SARS-CoV test; otherwise, the employer must not let them enter the workplace. The above mentioned exception for package tour participants applies here as well. Please note that unlike under

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the previous emergency measure, the obligation to submit a second test at the time of taking up employment has been dropped.

The arrival of foreigners may also be complicated by continuing limited operation of embassies. Since the beginning of August, the Ministry of Foreign Affairs of the Czech Republic has reopened most Czech embassies abroad, but many of them continue to operate in limited mode only. In some countries, the submission and approval of applications may therefore continue to be delayed. The embassy in Chile remains closed until further notice.

Considering the development of the epidemiological situation, it can be assumed that the rules for both entering the Czech Republic and the functioning of embassies abroad are not final. The situation needs to be closely monitored and assessed, especially as changes are taking place very quickly and their interpretation is not always clear.

How to prepare for the amendment to the Corporations Act

On 1 January 2021, an amendment to the Corporations Act will enter into effect, bringing a number of changes to corporate law. Most of the mandatory provisions of the amended law will be enforced against provisions of founding documents that are in conflict with them. The parallel existence of outdated provisions in founding documents and the new rules may cause complications in practice, which is why it is advisable to make appropriate amendments to memoranda of association and statutes.



Aneta Boukalová
kpmg@kpmg.cz



Roman Kuchař
kpmg@kpmg.cz

Although the amendment stipulates the general obligation to adapt the founding documents within one year of the amendment's effective date (and to file them in the Collection of Deeds within the same deadline), for the sake of legal certainty we recommend making the appropriate changes by the end of this year. It is also possible to time them to enter into effect together with the amendment. The scope of the necessary or suitable changes must be determined individually after a detailed review of each corporation's founding legal act. Some of the novelties to be taken into account for limited liability companies and joint-stock companies are listed below.

The most significant changes will concern the statutes of joint-stock companies that have chosen a monistic internal structure consisting of a statutory director and an administrative board. The office of the statutory director will be abolished and its responsibilities will be assumed by the administrative board performing the role of a statutory body with supervisory powers.

Many founding legal acts will have to be updated as their wording had literally been taken from the text of the law. In such cases it would be appropriate to replace that wording with a general reference to applicable legal regulations, otherwise it might be necessary to update them each time the law is amended. In the context of the current legal amendment, this concerns, e.g., a change to the scope of powers of the general meeting. The amendment also allows for various additions to be made to take better account of the relationships between partners/shareholders: for instance, it will be possible to attach the right to appoint and remove certain members of elected bodies to a particular business interest/share.

With the end of the year approaching, now is the time for a thorough review of an entity's founding legal acts; however, the amendment reaches much further, as depending on the circumstances, it may also be appropriate to modify partner/shareholder agreements or internal documentation (such as executive service agreements). Members of elected bodies should be well acquainted with changes in their rights and obligations; this is particularly true for members of statutory bodies as regards stricter obligations in the event of insolvency. It is also advisable to consult with legal advisors on ordinary matters in the business corporation's life (e.g. organisation of the general meeting), as the routinely followed procedures and documentation may no longer meet the new requirements.

Please note that if the amendment stipulates a duty to register in the Commercial Register any facts that have not

yet been subject to registration, the application for their registration must be filed by 30 June 2021, with some exceptions. The same deadline applies to documents that under the new rules have to be filed in the Collection of Deeds.

AML changes about to be finalised

Although the deadline for the implementation of the fourth and fifth AML Directives has already expired, the Czech Republic has not yet adopted adequate implementing regulations and is now facing infringement proceedings from the European Commission. Both legislative proposals should therefore be adopted swiftly. The new Act on the Registration of Beneficial Owners, and a major amendment to the AML Act and related regulations are heading to their second and third readings in the chamber of deputies.



Linda Kolaříková
lkolarikova@kpmg.cz
+420 222 123 889



Jiří Stratil
jstratil@kpmg.cz

The first bill introduces significant changes to the AML Act. These include: an extension of the range of obliged entities; changes to the process of client identification and review; a reform of administrative punishments; changes to the scope of powers of supervisory authorities; and a change in the data collected in the central accounts.

To better meet EU requirements, the register of beneficial owners will be moved to a separate piece of legislation. So far, the regulation has been fragmented between the AML Act and the Public Registers Act. Among other things, the new law introduces the publishing of certain data on beneficial owners and substantial penalties for non-compliance with certain registration obligations. Substantial changes are being made to the beneficial owner definition, and some problematic issues are being regulated in more detail.

Because of the above mentioned sanctions that obliged entities face should they fail to comply with their responsibilities under the AML Act ([for more information, refer to article here](#)), we recommend checking the setup of internal processes in the client review/monitoring area, i.e. whether they are in line with the new legislation and with the standpoint of the administrative bodies; for example, the Financial Analysis Office has recently further adapted the rules for the identification of minors.

The amendments will also affect the regulation of trusts; under the new bill, the determination of the beneficial owner will differ from the current concept.

We will be happy to advise you on what to watch out for upon transitioning to the new legislation, and what deadlines to observe when making the data registered in the register of beneficial owners compliant with the new regulations.

Landmark case-law: softer penalties for transfer prices incorrectly set by companies receiving investment incentives

The Supreme Administrative Court (SAC) has issued a ground-breaking judgment for companies drawing investment incentives under older schemes. The court confirmed that the failure to meet the condition not to increase the tax base for calculating tax relief by related-party transactions should not lead to a complete loss of investment incentives but just to a reduction of the tax relief claimed.



Karin Stříbrská
kpmg@kpmg.cz



Eva Trsková
kpmg@kpmg.cz

The Income Tax Act (ITA) as effective until 30 April 2015 contained a provision under which taxpayers receiving investment incentives who failed to comply with the condition not to increase the base for calculating the tax relief by related-party transactions in a manner not compliant with the economic principles of normal business relations shall lose the entitlement to the relief. The taxpayers were obliged to file additional tax returns for all taxable periods in which they had claimed the tax relief.

The harshness of this condition was mitigated by an amendment to the Income Tax Act effective from 1 May 2015, to the effect that the entitlement to tax relief in the taxable period in which the condition was not observed shall be reduced. The amount of the reduction shall be the product of the tax rate (19% corporate income tax rate) and the part of the change in the tax base that arose from the incorrectly set transfer prices between related parties.

The transitional provisions of the amendment then stipulated that the mitigating consequences of non-compliance would also apply to proceedings concerning investment incentives initiated before the amendment's effective date. However, the transitional provisions did not address whether they should also be applied to cases where the condition was breached before 1 May 2015.

The SAC has now answered this question, stating that since the transitional provisions do not contain any special rules for individual investment incentive schemes, even breaches of the condition not to increase the base for calculating the tax relief by transactions effected between related parties in the periods prior to the amendment's effective date shall be governed by the amended law. Consequently, the failure to meet the condition will have the effect of reducing the tax relief claimed, rather than losing the investment incentives altogether as per the original wording of the law.

SAC: Justifiable grounds for waiving penalties broader in practice than specified in GFD guidance

In its recent judgment, the Supreme Administrative Court (SAC) held that, when interpreting justifiable grounds for waiving penalties for the failure to report exempt income, administrative bodies must examine the specific circumstances of each individual case. If the list of justifiable reasons in the GFD's methodological instruction does not provide for a particular situation, this does not automatically mean that the penalty cannot be waived.



Jana Fuksová
jfuksova@kpmg.cz



Aneta Boukalová
kpmg@kpmg.cz

In the case in question, the SAC examined in more detail the interpretation of the provisions of the Income Tax Act allowing the tax authority to waive the penalty for the failure to report exempt income if such a failure occurred on grounds justifiable in the light of the circumstances of the case. The penalty amount ranges between 0.1% and 15% of the unreported income.

The involved taxpayer had sold his ownership interest in a corporation, which was exempt from tax, but without submitting a notice of exempt income of natural persons until called upon by the tax administrator. As a result, the obligation to pay a penalty of 10% of the sum of exempted income arose to this taxpayer. The taxpayer asked for a waiver of this penalty on the grounds that his health had deteriorated sharply, with him having to undergo dialysis several times a week. However, the tax administrator did not find this reason justifiable, referring to the GFD's Instruction D-28 that specifies four justifiable reasons. It concluded that the facts alleged by the taxpayer did not constitute any of the grounds specified in the guidance.

According to the SAC, the waiver of a penalty is not an option in a situation where the notice has not been filed intentionally or on the grounds of passivity or irresponsibility. On the other hand, the court also stated that the law intentionally does not specify justifiable reasons, to allow the administrative bodies to respond to the specific circumstances of individual cases. The GFD's methodological instruction is not relevant for subsequent judicial review purposes. Hence the court concluded that in the given case, the described health problems of the taxpayer could be regarded as serious enough as to constitute justifiable grounds for the waiver of the penalty for the failure to comply with the above reporting duty.

In practice, the judgment along with its commentary may affect not only the waiver of the penalty for the failure to report exempt income but also the assessment of circumstances for the waiver of default interest, interest on the deferred tax amount and the penalty for failure to file a VAT ledger statement where the legislation and related GFD's methodological guidance have been constructed in a similar manner. When waiving such sanctions, the tax authorities should always take into account the individual circumstances of the case and consider whether they constitute justifiable grounds. The GFD's interpretation contained in the instruction can only help deal with the issue but cannot cover all conceivable life situations.

SAC on deadline for correcting the VAT amount and on appealing against implicit tax assessments

In a recent judgment, the Supreme Administrative Court (SAC) held that it is possible to correct the VAT amount within three years of the end of the taxable period in which the tax liability arose, whereas it is not possible to appeal against implicit tax assessments.



Veronika Výborná
vvyborna@kpmg.cz



Zuzana Černá
zcerna@kpmg.cz

A taxpayer has filed additional VAT returns for several quarterly taxable periods from 2011 to 2013 in which the entity reduced the originally-reported value of effected taxable supplies to zero to correct the tax amount. These additional VAT returns were filed in connection with parallel tax proceedings concerning personal income tax. Within these proceedings, the tax authority reclassified the income initially regarded as supplies effected within the economic activity to income from dependent activity (employment). The taxpayer disagreed with the tax authority's conclusions. However, to avoid the expiration of the appropriate VAT taxable periods, the taxpayer filed the above additional VAT returns along with an explanatory letter expressing its objections against the reclassification and challenging the VAT amount asserted in the filed additional VAT returns.

Deadline for correcting the VAT amount

The SAC declared that it is possible to correct the VAT amount within the three years of the end of the taxable period in which a duty to declare VAT on the original supply arose. Within these three years, it is necessary to issue a corrective tax document (which must be delivered to the other party, or to make a correction in the VAT records) and to file an additional VAT return. The SAC's judgment also comments, among other things, on a disputable taxable period involving the first quarter of 2011, which ended on 31 March 2011. The three-year period therefore expired on 31 March 2014. Until that date, when correcting the VAT amount pursuant to Section 43 of the VAT Act, it had been necessary to file an additional VAT return. According to the SAC, the deadline for correcting the tax amount pursuant to Section 43 of the VAT Act differs from the deadline for correcting the tax base pursuant to Section 42 of the VAT Act. The SAC's extended panel of judges is currently discussing the deadline for correcting the tax base pursuant to Section 42 of the VAT Act in another case. We will keep you informed about any developments in this matter.

Appeal against implicit tax assessment

In its judgment, the SAC also opined on the possibility to file an appeal against an implicit tax assessment, i.e. when the tax administrator agrees with the tax asserted by the taxpayer and does not issue a tax assessment. The SAC concluded that no appeals can be filed in such cases. However, if, after additional tax returns have been filed, the tax administrator initiates a procedure to remove doubt (or subsequently a tax inspection), an appeal is admissible even if the additionally-assessed tax in the tax assessment does not differ from the tax asserted by the taxpayer in an additional tax return.

The SAC concluded that where taxpayers have a chance to challenge the asserted tax by filing additional tax returns, they may not challenge their own tax assertion by submitting an appeal along with the tax return forms.

SAC: Substantiating the performance of R&D activities is essential to claim an R&D allowance

According to the Supreme Administrative Court (SAC), when proving the development activity for the purposes of claiming an R&D allowance, it must be clear from the evidence how existing knowledge or skills were systematically applied and tested to design a new or improved product, process or service. Only then is it possible to verify whether the taxpayer carried out a genuine development activity and not just their normal production on the basis of customer requirements.



Michaela Thelenová
mthelenova@kpmg.cz



Barbora Halatová
bhalatova@kpmg.cz

In the 2013 income tax return, a taxpayer claimed a research and development allowance. The R&D project at issue was directed to the manufacturing industry (construction and production of equipment). To the tax administrator, the taxpayer submitted project documentation defining the project's goals and containing an annual assessment report and technical documentation including a technical report and an expert opinion. However, this was not sufficient for the tax administrator, arguing that the taxpayer did not prove that the project had involved experimental development and not just pre-production preparation or innovation. The Regional Court agreed with the tax administrator's conclusions that the taxpayer did not prove the performance of activities leading to research and development results. In the court's opinion, it was not enough for the outcome of the activity to be a new solution; the important thing was whether and how the research and development leading to this new solution was carried out. The decisions of both the administrative authorities and the Regional Court were based on the taxpayer's failure to provide documentation supporting the course of the development process.

The taxpayer appealed against the Regional Court's decision, claiming that if a final R&D product as well as documentation enabling the production and use of such a product and a technical report describing the product exist, there should be no need for providing further evidence of the process through 'project work documentation'.

According to the SAC, the basic pre-requisite for claiming an allowance for experimental development is the provision of documentation supporting the activity. The most suitable tool to do so is documentation capturing the process of creating a new or improved solution. The taxpayer argued that if what was created by the activity was new and unique, that result must have necessarily been preceded by research and development. However, according to the SAC, this is not correct, as the novelty and uniqueness of the device does not mean that it was created as the result of a development activity. Moreover, the submitted expert opinion was not found to be convincing evidence in the given situation either, since the expert's conclusions had not been properly substantiated and the evidentiary value of the expert opinion was also undermined by the expert's testimony. The court thus dismissed the cassation complaint as unfounded. The question of whether any research and development was involved is above all an issue of providing sufficient supporting documentation.

Is it possible to deduct VAT on induced investments?

The Court of Justice of the EU (CJEU) in the recent *Mitteldeutsche Harstein-Industrie AG* case (C-528/19) dealt with whether it is permissible to deduct input VAT on construction work carried out on a municipal road for the benefit of a municipality, and whether building a municipal road constitutes a supply of goods for consideration.



Martin Krapinec
mkrapinec@kpmg.cz



Marcela Jelínková
kpmg@kpmg.cz

A German company wanted to open a limestone quarry whose operation was permitted by the local government authority on the condition that a public road belonging to the municipality would be built to the quarry. The company agreed to cover all costs of building the road. The municipality promised that the company would be allowed to use the road for heavy trucks accessing the quarry, without any limitations.

The court first dealt with the question whether the company was entitled to deduct VAT in respect of the work carried out to build the road for the benefit of the municipality. The CJEU pointed out that without building the municipal road, it would have been impossible to operate the limestone quarry, from both a practical and a legal point of view. The construction work on the municipal road was therefore essential for the company to carry out its economic activity, i.e. to operate the limestone quarry. The fact that the road was also available to the public free of charge, was irrelevant, as the road was built primarily for the purposes of the quarry operator (access of heavy trucks), not for the purposes of the public. The CJEU thus concluded that the company was entitled to deduct VAT on the work carried out to construct the municipal road, to the extent that the work had been essential for the company's economic activity.

In its answer to further questions referred to it, the CJEU stated that the authorisation to operate a quarry granted unilaterally by the government authority cannot be deemed a consideration received by the company for carrying out the construction work on the municipal road. The CJEU pointed out that a unilateral act by a public authority cannot establish a legal relationship entailing reciprocal performance. Furthermore, the work on the construction of the road cannot be considered a supply of goods to the municipality for consideration, even though the municipality benefited from the construction, as the road was built primarily for the purposes of the quarry operator.

CJEU rules on adjustment of deductions claimed for capital assets

What is the situation as regards the modification/correction of VAT deductions claimed on capital assets if their use changes? And what if the assets have not yet been used but their intended use has changed? These were some of the issues the Court of Justice of the European Union (CJEU) dealt with in its latest judgement.



Tomáš Havel
thavel@kpmg.cz



Petra Němcová
pnemcova@kpmg.cz



Marcela Hýnarová
kpmg@kpmg.cz

In Dutch case C-791/18 *Stichting Schoonzicht*, the applicant in the main proceedings had had an apartment complex comprising seven residential apartments built on their plot of land in 2013 and 2014. The completed project was delivered to them in July 2014. As the apartment complex was from the beginning intended for the provision of taxable supplies, the owner deducted, in full, input VAT charged to them for the construction of the complex in 2013. However, in August 2014, the applicant leased some of the apartments in a VAT-exempt regime, while the remaining apartments remained unoccupied. Under Dutch VAT legislation, the tax administrator requested a refund, in full, of the originally claimed VAT for the leased apartments.

The applicant objected to the tax administrator's approach, arguing that Dutch legislation was contrary to the VAT Directive, namely Article 187, stipulating that in the case of capital assets, any adjustment shall be spread over five years including the year in which the goods were acquired or manufactured.

The CJEU did not accept the applicant's arguments, stating that the article referred to does not cover situations where the entitlement to a VAT deduction is lower than originally reported, and this becomes apparent already when the assets were first used.

The CJEU held that Dutch legislation is not contrary to the directive. Under Dutch legislation, it is possible to request of a taxpayer to make a one-off adjustment/correction of the full amount of the deduction claimed if the change in the use of the immovable property, and, at the same time, the adjustment/correction of the deduction took place in the year of its first use.

Following the above, we recommend properly documenting the intended use of capital assets, and archiving the documentation over the entire time when a tax inspection may be possible. Especially in periods of economic downturn, original investment plans may change significantly.

CJEU approves French approach to regulating short-term leases

The Court of Justice of the European Union (CJEU) has sanctioned a French legal provision requiring in certain locations the prior authorisation by local authorities for short-term leases – typically leases arranged through digital platforms.



Linda Kolaříková
lkolarikova@kpmg.cz
+420 222 123 889

While the previous Airbnb judgment (C-390/18) dealt with the admissibility of regulating platforms mediating leases, the September CJEU judgment in the joint cases of Cali Apartments (C-724/18 and C-727/18) deals with the possibility of regulating providers of accommodation.

The main point of contention of the disputed French regulation has been that obtaining official consent is conditional upon the concurrent conversion of (other) non-residential premises to premises for housing.

The judgment is largely based on the opinion of Czech Advocate General Michal Bobek. According to the CJEU, the case falls within the scope of the Service Directive. At the same time, the public interest – in this case, affordable long-term housing – can justify a state’s intervention. However, the detailed arguments of the judgment make it clear that it is for the national courts to carefully monitor the proportionality of the authorities’ discretion.

At the European level, the sector at issue will also be affected by the [Digital Services Act](#).

News in brief, October 2020

Last month's tax and legal news in a few sentences.



Lenka Fialková
lfialkova@kpmg.cz



Václav Baňka
vbanka@kpmg.cz

DOMESTIC NEWS IN BRIEF

- The Personal Data Protection Office imposed a sanction of CZK 6 million for the repeated unsolicited distribution of commercial communications. It is the highest penalty for this type of wrongdoing imposed during the office's existence.
- According to the CJEU's judgement (C-422/19 and C-423/19), creditors in general must accept cash to repay monetary debt.
- The government's proposal to introduce a lump-sum tax for the self-employed passed through the first reading in the chamber of deputies. The annual income generated from business activity that can be subject to this regime may not exceed CZK 800,000. The lump-sum tax will allow self-employed persons to settle their income tax liability plus social security and health insurance obligations through one lump-sum payment, without having to complete three different prescribed forms.
- An act abolishing the immovable property acquisition tax with a retrospective effect from December 2019 has been promulgated in the Collection of Laws. The financial administration has published several communications on this, as well as illustrative examples and a tax refund application template.
- A decree determining the extent of data and the method of their recording in the register kept pursuant to the Act on the Promotion of Sport has been published in the Collection of Laws (373/2020).
- A government decree on the amount of the general assessment base for 2019, the recalculation coefficient for adjusting the general assessment base for 2019, the reduction limits for determining the calculation base for 2021 and the basic amount of pension for 2021, and on increasing pensions in 2021 has been published in the Collection of Laws (381/2020). The data specified in the decree affect the amount of retirement pensions, the maximum assessment base for mandatory contributions to the social security scheme, and the minimum amount of social security and health insurance prepayments for self-employed persons.
- The Ministry of Foreign Affairs has negotiated a double taxation treaty and a related protocol between the Czech Republic and Ghana (38/2020).

FOREIGN NEWS IN BRIEF

- The European Commission has published its draft [Digital Operational Resilience Act](#), aimed at enhancing the cybersecurity of financial institutions and strengthening their readiness against cyber-attacks.
- The European Commission has decided to appeal the General Court's judgment on the Apple State aid case in Ireland before the Court of Justice of the European Union.
- In the European Parliament's budget committee, EU lawmakers backed a bloc-wide charge on unrecycled plastics and called for a timetable for the introduction of digital and financial transaction taxes, among others, to help fund the EU budget.
- For changes to tax legislation in 2021, the Polish government is planning, among other things, to abolish the tax transparency of limited partnerships and some general partnerships, to introduce the obligation of certain corporate taxpayers to prepare and publish their tax policy and changes in transfer pricing policy, to extend the scope of transactions for which transfer pricing documentation will have to be prepared and to

expand the documentation's content.

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www.kpmg.cz

Tel.: +420 222 123 111

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