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Editorial

The tornado disaster in South Moravia has again shown that Czechs can rally to each other's help when necessary. The money that is being collected in fundraisers to help the people and communities affected by the natural catastrophe is breaking records, and I am happy to say that we at KPMG have also done our bit. In a firm-wide effort, we collected nearly CZK 450 thousand, and many of my colleagues also contributed individually. KPMG will double the amount collected. Above all, I am especially proud of my colleagues from the Brno office, who did not hesitate to travel to the affected municipalities to help with the clean-up. After all, Brno is just a short drive from Hodonín, and we have families, friends and clients there.

On the tax news front, we are happy to report that the tax package remains valid even though the president has not signed it. This was confirmed by the Constitutional Court, as it rejected a petition by a group of senators to annul the law. Because of the absence of the president's signature, there were some doubts about the constitutionality of the process of adopting and promulgating a law that, among other things, abolished the super-gross wage and introduced progressive taxation. I think the court's decision is good news, as a stable tax environment is what we really need.

It also turns out that the tax authorities are still on the alert and have not hesitated to initiate tax inspections even during the COVID-19 pandemic. Neither have they wavered to impose sanctions after such inspections. But did you know that you can apply with the tax administrator to waive part of the penalties? However, such a waiver is conditional upon a taxpayer's good payment discipline and collaboration during the tax inspection. In this issue's Tax Tips and Tricks section, you can find out how to get the highest penalty waiver possible, i.e. up to 75% of the fine.

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Amendment to VAT Act 2021: EU directive's direct effect applicable in majority of e-commerce spheres

An e-commerce amendment to the EU VAT Directive has been in effect since 1 July 2021. Unfortunately, the Czech Republic has not yet implemented it: the relevant amendment to the Czech VAT Act is still awaiting approval by the Senate. In its recently published information, the General Financial Directorate (GFD) attempts to provide clues on how to proceed after July, as it should be possible to apply the direct effect of the directive to most areas.

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In its information, the GFD confirms that until an amendment to the Czech VAT Act enters into effect, it is possible to proceed in compliance with the current wording of the act or apply the direct effect of the amended EU directive.

The fundamental question is what areas, and to what extent, will be affected by the **Czech** amendment not having been adopted and effective. An important change to be introduced by the amendment is the cancellation of taxation thresholds for individual member states from 1 July 2021: until now, dispatched goods costing less than the set threshold were taxed in the country of dispatch. If the place of taxation is in another EU member state, the duty to tax the goods in the country of the end recipient in another member state will by no means be affected by a delay in the legislative process in the Czech Republic. The question is whether it will be possible to use a one-stop-shop (OSS) in the Czech Republic for tax settlement purposes even before the Czech amendment's effectiveness. The GFD's information allows for this option, which makes us believe that the one-stop-shop mechanism is already fully operational. It has been possible to register for the OSS from April 2021.

Since Czech payers sending goods to end customers in the EU must continue to declare the tax bases for their sales in their Czech VAT returns even if they use the OSS, the GFD also clarifies this procedure. The amendment also changes VAT return forms: the sales in question will be declared in line 24.

For imports of low-value consignments, the current exemption from VAT for consignments costing less than EUR 22 will remain in effect until the Czech amendment's effectiveness. This shall also apply to imports using the import-one-stop-shop (IOSS) mechanism.
The GFD also provides information about the direct application of the directive to distance sales of goods and distance sales of imported goods that are facilitated by electronic interfaces (platforms).

The customs administration has also issued important information about the link between VAT registration and the duty to file Intrastat reports. If an EU or third-country supplier is deregistered from Czech VAT in connection with using the one-stop-shop, the duty to file Intrastat reports ends in the month in which the registration is cancelled. However, it should be noted that this is not a matter of course in other member states. We therefore recommend reviewing the conditions for filing Intrastat reports in the member states in which the supplier is

deregistered for VAT. So far it seems that certain member states will require the filing of Intrastat reports even when VAT registration is cancelled and tax is to be settled within the one-stop-shop.

Second call under COVID – Uncovered Costs programme

The Ministry of Industry and Trade has prepared a second call to participate in the COVID – Uncovered Costs programme, aiming to compensate for fixed costs incurred by entrepreneurs reporting significant decreases in sales compared with the period before the COVID-19 pandemic. Applications for support may be filed from 28 June 2021.

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The basic condition for awarding support is a decrease in sales for the relevant period of 2021 by at least 50% compared with the same period in 2019. This is a change from the first call of the programme (discussed in this article), under which the decrease in sales was compared with a comparable period in either 2019 or 2020.

The relevant period for second-call purposes is 1 April to 31 May 2021. Where applicants cannot prove a sufficient decrease in sales for the entire relevant period but did suffer a decrease of more than 50% in April 2021, it is possible to claim just this month as the relevant period.

As under the first call, support shall amount to 60% of uncovered costs for the relevant period (or 40% for applicants with any ownership interest held by the state or local self-government). Again, it is necessary to prepare an adjusted income statement for the relevant period in accordance with the call's requirements. Uncovered costs shall mean losses net of subsidies as specified by Section 3.1 of the European Commission's Temporary Framework, i.e. Antivirus A, B, A Plus and other subsidies for eligible expenses. Where losses net of subsidies exceed CZK 5 million, applicants will have to submit an adjusted income statement (prepared in accordance with the call's requirements) verified by their auditor.

The maximum subsidy amount is CZK 25 million (or CZK 15 million, where applicants chose April 2021 as their relevant period) or the amount of the undrawn subsidy determined during the first call. Applications shall again be filed via the Ministry of Industry and Trade's electronic system.

Even though the deadline for filing applications does not end until 13 September 2021, considering our experience with previous calls we recommend submitting applications sufficiently in advance before the deadline to avoid any possible technical problems caused by system overloads in the last days before the call's closure.

Tips and tricks

Minimising penalties - how to claim a waiver?

Depending on the results of a tax inspection, a penalty of 20% of the additionally assessed tax or 1% of the amount by which a tax loss was reduced may become due. This amount is fixed, and cannot be reduced by tax administrators on their own. However, the penalty may be waived, up to 75%, based on the taxpayer's request. In justified cases, the final penalty may thus drop to 5% of the additionally assessed tax or the amount by which the tax loss claimed was reduced. Below we summarise the conditions and procedure for claiming the waiver.

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How to apply for a waiver?

The application for a waiver of penalty is subject to an administrative fee of CZK 1,000 (unless the amount to be waived is less than CZK 3,000) and must be filed within three months after the order to pay the additionally assessed tax has entered into effect. This means that if an appeal has been filed against the order, the application shall only be filed once the appeal procedure has been closed. The waiver of the penalty is conditional upon the payment of the additionally assessed tax: the tax does not have to be paid at the time of applying for the waiver, rather at the time when the application is being assessed by the tax authority. At this point, the penalty itself does not have to be paid, but until it is waived, it remains a due and payable liability, which may have negative implications when applying for subsidies, etc. This can be eliminated by applying for a penalty payment deferment on the grounds of the expected waiver. It is also possible to pay the penalty and, once the waiver is granted, apply for a refund of the overpayment; this is necessary, as the tax authority does not refund overpayments automatically.

While the tax authority does not provide a form that should be submitted, it recommends that the application specify who is applying, to whom it is addressed, and what its subject is. A successful application should also contain a rationale stating the arguments for the waiver.

How much can be waived?

When deciding on the application, the tax authority in particular follows General Financial Directorate Instruction D-47. In accordance with the instruction, they first check that the necessary preconditions for granting the waiver have been met. After that, they decide on the amount of the penalty to be waived.

A waiver will not be granted if the taxpayer or its statutory body (typically a statutory representative of a limited liability company or a member of the board of directors of a joint stock company) has grossly violated tax or accounting regulations in the last three years. This means that a waiver will not be granted to 'unreliable VAT

payers', perpetrators of tax-related crimes, or those who have not filed their tax returns on time two or more times in the last 12 months while being called upon by the tax administrator to do so.

The amount of the waiver is determined by the extent of the taxpayer's collaboration in the additional tax assessment. This does not mean that taxpayers should not defend themselves or not be active during the tax inspection. On the contrary, a passive and uncollaborative approach – not responding to calls, not submitting required documents, not allowing the initiation of the tax inspection, concealing evidence – may result in a lower amount of the waiver: for any such conduct, the amount waived shall be reduced by 20 to 100%.

The last criterion to be assessed is the frequency of breaches of duties in tax administration. This means, for instance, whether the taxpayer has been fined under the Tax Procedure Code two or more times in the last three years, or whether any other tax arrears are being enforced against them. These circumstances reduce the penalty's waivable portion by a further 50%.

Penalty waivers can be an efficient way to minimise the costs associated with additional tax assessments. The conditions of the waiver have been set up to motivate taxpayers to duly meet their obligations and collaborate during tax inspections.

Labour Inspection Office focuses on illegal employment and unlawful labour hire practices

Illegal work and concealed agency employment are offences associated with the highest sanctions in the labour-law sphere, as the Labour Inspection Office may impose fines of up to CZK 10 million on employers. The office has been focusing on identifying this type of misconduct quite intensively and imposed high penalties also in 2020.

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Despite complications associated with the COVID-19 pandemic, last year the Labour Inspection Office carried out more than five and a half thousand inspections focusing on illegal employment, revealing more than three thousand illegal workers, mainly from countries outside the EU, even though the pandemic itself had generally decreased the number of foreign nationals in the Czech Republic. The average penalty amounted to CZK 240 thousand.

Illegal work may take on two forms: employment of foreigners without appropriate work and residence permits and the so-called 'Svarc' system, i.e. performance of dependent work outside an employment relationship. Illegal employment of foreign nationals does not only involve not having any permits at all but also cover situations when foreigners have permits that do not apply to the type of work they are performing. Employers most often forget to apply for a change of permit upon a change of position or place of work. Regarding the 'Svarc' system, it is now less common for employers to pursue the conclusion of contracts other than employment contracts; instead, job candidates themselves are often interested in more flexible arrangements. But when it comes to setting out mutual contractual rights and duties, they do not know their way around and instead enter into arrangements that resemble employment relationships.

Apart from "traditional" illegal employment, inspectors increasingly often come across a more recent unlawful structure: concealed agency employment. This involves situations when an entity offers its employees' work for consideration without having an employment agency licence necessary for such a business. In the last year, the number of penalties imposed for concealed agency employment was lower but the average penalty amount was significantly higher, exceeding CZK 450 thousand. This type of offence is relatively new and many companies are not even aware of having been engaged in it. The line between legally providing services through employees and lending employees to fulfil customers' instructions is indeed relatively thin, with a decisive role being played by the conditions of the collaboration and the contractual provisions.

The Labour Inspection Office's statistical figures for the previous year are in line with our experience from practice. The complexity of immigration procedures and the inflexibility of labour-law regulations often drive employers to consider more risky but more flexible solutions. For concealed agency employment / employment mediation, the problem lies with the relatively complex concept, where the difference between legal and illegal

arrangements often seems mere legal wordplay to pragmatists. A sensitive legal review of contracts on cooperation with self-employed persons or contracts based on which employees work for customers may bring significant benefits and improve this year's statistics.

Amendment to Foreigners' Residence Act not passed by Senate

In mid-June, the Chamber of Deputies approved the long-awaited bill to amend the Foreigners' Residence Act and passed it on to the Senate. On 1 July, the Senate rejected the amendment. Below, we present the changes that the amendment was intended to bring, and the controversial issues that made the Senate reject it.

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An immediately visible and significant change concerns **Brexit, and the adaptation of the withdrawal agreement into Czech law**. The law now reflects the principles and rules enshrined in the agreement: among other things, the amendment regulates the status of UK nationals who legally resided in the Czech Republic during the transitional period and whose stay continues after its end. The law also addresses the status of their family members, and the documents to be issued to UK nationals and their family members.

Perhaps the biggest and most complex change concerns **family members**. The definition of a family member of an EU or Czech citizen has changed and is now more specific in its individual categories and gives less space to unclarity in the interpretation of the law. At the same time, the amendment introduces a completely new definition of family members of UK nationals, defining the conditions for obtaining the status of beneficiaries of the withdrawal agreement.

The third major change previously announced is **the replacement of current residence permits for UK nationals and their family members with biometric cards**. We expect the Ministry of Internal Affairs in charge of this agenda to publish more details. The original bill of 2020 also envisaged this replacement for other EU citizens and their family members, however, the current wording only covers UK nationals.

EU citizens and their family members will also be affected, as their existing documents will remain valid, but newly issued temporary residence certificates will now be called **registration certificates**. We expect that the existing application form will be modified accordingly. Nonetheless, apart from the name change, no other significant changes are expected.

The amendment also brings **a few minor changes**. For instance, in the application for a temporary residence permit for a family member of an EU citizen who is not a direct family member, it will be necessary to provide a certificate of sufficient income.

The amendment's wording, while approved by the Chamber of Deputies, was subsequently rejected by the Senate. The main reason was the controversial regulation governing the compulsory insurance of foreigners with the General Health Insurance Company (Všeobecná zdravotní pojišťovna - VZP). The regulation had been criticised not

only by the senators, but also by the Ministry of Health, the Chamber of Commerce and the Office for the Protection of Competition.

The amendment thus now returns to the Chamber of Deputies. Its approval will require a simple majority of all deputies. We will follow the future fate of the amendment and hopefully will be able to present to you its final wording in one of the future issues of the Tax and Legal Update.

Registration of beneficial owners' first month

The Act on the Registration of Beneficial Owners, a ground-breaking legal regulation, entered into effect on 1 June 2021. Since this date, the registry of beneficial owners has been available to the public and allows individuals to obtain a partial copy of data contained in the registry. Owing to strict penalties and other adverse implications, the registration of their beneficial owners has become an urgent matter for many companies.

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From the public part of the registry it is now possible to obtain certain information about beneficial owners (e.g. name and address, position and date on which a person became the beneficial owner). It is therefore also possible to ascertain which companies have not yet registered their beneficial owners.

Companies whose beneficial owners are already clearly identifiable from the Commercial Register ("CR") do not have to file a petition for registration, as the data from the CR is automatically transferred to the registry of beneficial owners. However, they must make sure that the data transferred from the CR are true and up-to-date. If not, they have to ensure that appropriate changes are made.

The automatic transfer of data does not apply to companies that have filed a petition for the registration of a beneficial owner any time in the past. If these companies are interested in the automatic transfer, they must first ask the court or notary.

The data registration, or any changes to such data, can be performed through the courts or notaries. It is clear from the new law and related regulations that the legislators meant to motivate companies to register their data through notaries, as such registration is less formal, quicker and cheaper.

We already informed you about the sanctions for the failure to register beneficial owners within the set deadlines, such as the inability to exercise voting rights at general meetings, restrictions on the payment of shares in profit and other own resources (equity payments), or financial sanctions. However, companies failing to register or update their beneficial owner data in a proper manner may also face other adverse practical implications, such as their inability to acquire notarial deeds regarding certain legal acts (following from their inability to vote at general meetings) or complications with maintaining and opening bank accounts. This may ultimately result in their inability to properly function and operate. The companies have therefore no choice but to register their beneficial owners as soon as possible.

Beware of new standard contractual clauses when transferring personal data outside the EU!

The European Commission has adopted two implementing regulations with significant impact on personal data processing. Effective from 27 June 2021, it is possible to use new standard contractual clauses for transferring personal data from the EU/EEA to third countries and new standard contractual clauses for contracts on personal data processing between controllers and processors. This further strengthens the protection of personal data, especially with respect to its processing in third countries.

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Contractual clauses for personal data transfers from the EU to third countries

The new standard contractual clauses for transferring personal data from the EU/EEA to third countries are the first clauses of this kind adopted under the GDPR's effectiveness, responding to the decision of the Court of Justice of the EU from July 2020 holding the EU-US Privacy Shield invalid, thus making any transfers of personal data to the USA more difficult. The contractual clauses should provide suitable guarantees for the transfer of personal data, respond to society's shift towards digitalisation, ensure higher flexibility upon personal data transfers, and be easily available to a greater number of persons.

The clauses interconnect the general provisions with individual scenarios (modules) for transferring personal data between third-country controllers and processors who may choose the scenario (from the outlined ones) that suits them best in a particular case (personal data transferred between two controllers, a controller and a processor, a processor and a controller, or between two processors), giving them chance to adjust their duties accordingly for each particular case. Compared with the standard contractual clauses that have so far been in effect, the new contractual clauses take into account a greater number of possible scenarios, covering also situations when personal data are transferred from the EU/EEA processors to third-country controllers or between a number of processors.

The new standard contractual clauses may be used from 27 June 2021; the existing clauses can be relied upon in certain personal data transfer cases until 27 December 2022. However, we recommend starting to update contracts with suppliers and customers containing these standard contractual clauses as soon as possible.

Clauses for personal data processing contracts

When transferring personal data within the EU and EEA, these new standard contractual clauses serve as templates for personal data processing contracts concluded between controllers and processors (potentially also other subsequent processors if chaining of processors is involved) in compliance with Article 28 (3 and 4) of the GDPR. The inclusion of these clauses in contracts shall mean the fulfilment of the GDPR's requirements on personal data

processing contracts while minimising the risk that personal data will be transferred to the processor without an existing or valid legal title.

Also allowing for the involvement of several persons, these clauses should mainly standardise the rights and duties of controllers and processors where personal data processing involves one or more processors. In their final effect, the clauses are meant to facilitate the existing process of entering into personal data processing contracts and, making it more efficient.

The new standard contractual clauses for personal data processing contracts can also be used from 27 June 2021. Considering the above, we recommend evaluating whether any existing personal data processing contracts meet GDPR requirements and, if they do not, making the necessary adjustments.

International taxation rules may change as early as 2023

In a joint declaration, 130 out of the 139 countries united under the OECD for the purpose of implementing the BEPS initiative have agreed on new rules for the international taxation of multinational corporations. The final wording of the rules, mainly responding to the global economy's digitalisation requirements, should be approved in October this year, with their effectiveness set as an ambitious goal for 2023. Countries that have showed their support include the world's largest economies, i.e. the USA, China, Germany, France and Russia.

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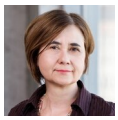

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The new rules are based on a two-pillar approach. Under Pillar One, profits shall be taxed in the country of the products' or services' sale (the market country) regardless of whether a group company selling the products or services is physically present in the market country. However, this shall only apply to multinational groups with a global turnover of more than EUR 20 billion and profitability above 10% (measured as profits before tax divided by revenue recognised in the consolidated financial statements). It should therefore apply to the approx. 100 largest multinational groups. The market countries will be entitled to tax the profits if the group's total sales in a particular country exceed EUR 1 million. The market countries meeting this requirement shall then be able to divide 20–30% of the residual profits, defined as profits above a 10% margin, among themselves. The key for allocating this part of profit among individual countries will be the share of revenues from a particular market in the total revenues of the group.

Pillar One rules will be implemented through a multilateral instrument impacting on double taxation treaties. The instrument should be prepared for signature as early as in 2022, to be in effect from 2023. The instrument should also stipulate the country's commitment to cancel any already existing unilateral digital services taxes. Financial services subject to regulation and the mining industry shall be excluded from the new rules.

Pillar Two will introduce the global anti-base erosion (GloBE) rules, ultimately having a far greater impact than Pillar One rules, as they apply to multinational groups with a turnover exceeding EUR 750 million. This pillar also contains the income inclusion rule (IIR) under which an additional top-up tax payable will arise in a group's parent company's country if the profits of group companies in any one country are taxed at an effective tax rate below a minimum tax rate. Pillar Two also contains the undertaxed payment rule (UTPR) under which it is possible to deny the tax deductibility of expenses where the payment recipient is a company in a jurisdiction with low taxation. The agreed minimum tax shall be 15%.

To illustrate, if the tax calculated as a proportion of the tax rate determined based on legislation of an individual country and accounting profits is lower than 15%, it will be topped up to this agreed amount at the parent company's level. The GloBE rules should be applied following the procedure agreed at the OECD level. The participating countries' declaration expects that the rules will already become effective in 2023.

The meeting of G20 finance ministers and central bank governors in October this year will host the potentially last

debate on these rules.

Companies to disclose income tax payment information

The European Commission has published a draft directive on the mandatory disclosure of information on income tax payments in individual member states and non-cooperative jurisdictions (public country-by-country reporting). The duty will apply to companies belonging to a corporate group controlled by a company established in or outside the EU with a consolidated turnover exceeding EUR 750 million.

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The Council and the Parliament of the EU have arrived at a political consensus regarding the legislative wording of a directive introducing the duty to disclose a report of income tax payments (the so-called public country-by-country reporting) via an amendment to Directive 2013/34/EU, on annual financial statements and consolidated financial statements.

Income tax payment reports will have to be published by corporate groups controlled by a company established in or outside the EU with a consolidated turnover exceeding 750 million and activities in more than one member state. Where a corporate group is controlled by an entity established outside the EU, this group must have a subsidiary undertaking established in the EU with a turnover of at least EUR 8 million or total assets exceeding EUR 4 million or 50 employees (at least two of the above conditions must be met).

Income tax payment reports will contain selected information for all group companies that have their registered office in an EU member state or a country listed among non-cooperative jurisdictions (including grey-listed countries, i.e. those being monitored by the EU). Reports shall disclose certain information such as information about business activity, number of employees, results of operations before taxation, and current and deferred corporate income tax, including comparable information for branches. Reports should be published on the companies' websites or in public commercial registers.

The final approval of the directive on the EU level is expected before the end of this year. The directive will then be published in the EU Official Journal and enter into effect on the 20th day after its promulgation. The EU member states will have 18 months to transpose it into their national legislations. If the directive enters into effect on, e.g., 1 October 2021, member states should implement it before 1 April 2023. In this case, income tax payment reports would have to be published for accounting periods started 1 April 2024.

Case law

Constitutional Court more flexible on non-compete clauses in employment contracts

In May, the Constitutional Court dealt with the possibility of employers to withdraw from non-compete clauses. This court has a more liberal view of the matter than the Supreme Court which believes that an employer's withdrawal without giving a reason is invalid, even if such an option was explicitly agreed upon between the employer and the employee. The Constitutional Court has now ruled such a conclusion to be excessive and infringing upon the employer's rights. The decision could bring relief to many employers.

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In the dispute in question, an employer and their employee had negotiated a non-compete clause under which the employee was not allowed to work for the employer's competitors for six months after the termination of their employment. For each month of this restriction, they were entitled to compensation equal to a half of their average earnings, and would have to pay a contractual penalty if the clause was breached. In the non-compete clause, the parties had agreed that the employer may withdraw from the clause, even without giving reason.

The employee gave their notice of termination, and, during the notice period, the employer used the option to withdraw from the clause without giving reason. The employee subsequently sought the invalidity of the withdrawal, invoking the Supreme Court’s case-law, and demanded payment of the compensation for observing the ban to compete. Ordinary courts sided with the employee: despite the explicitly agreed upon possibility of withdrawing from the clause without giving reason, the employer's withdrawal was held invalid. The courts primarily argued that withdrawal from the non-compete clause without giving reason may significantly infringe on the employee’s rights, as the withdrawal can be made, e.g., on the last day of employment, when the employee had already chosen their next job. The employer then brought the matter to the Constitutional Court.

The Constitutional Court held that a general impossibility for an employer to withdraw from a non-compete clause without giving reason was excessive, irrational, and infringing upon the employer's fundamental rights. Unlike the ordinary courts, the Constitutional Court emphasised the principles of autonomy of will and contractual freedom. At the same time, the court held that lifting the ban to compete was primarily in the interest of the employee, as the clause stipulated the employee’s obligation not to compete with the employer in their future economic activity and possibly also the obligation to pay a contractual penalty. Therefore, withdrawal from a non-compete clause cannot be automatically invalid.

The Constitutional Court nevertheless stressed that courts must continue to grant employees a higher level of protection against the arbitrary behaviour of employers. Therefore, the specific circumstances of a case should always be examined, especially whether the employer has not abused their right or acted arbitrarily. It will be necessary to take into account, among other things, when the withdrawal took place, the reasons for which the employer withdrew from the non-compete clause, and whether the employee chose their next job precisely with regard to the concluded non-compete clause.

The decision is a welcome liberalisation. It is the second ruling by which the Constitutional Court recently overturned the Supreme Court's strict approach to non-compete clauses. Please note that employees are not automatically banned from competing once their employment ends. If employers are interested in protecting their know-how, with their employees, they should conclude non-compete clauses that include reasons for possible withdrawals by either party.

Case law

Limits to shareholder agreement validity regarding board member instructions

In Judgment No. 27 Cdo 1873/2019-336, the Supreme Court (SC) dealt with the validity of clauses in shareholder agreements, making a significant contribution to the abundant case law concerning the boundaries between business and strategic management.

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The Supreme Court dealt with the validity of clauses of a shareholder agreement (SHA) giving shareholders the right to nominate a certain number of members to a company's board of directors. The SHA also stipulated the shareholders' obligation that if the company needed funds, the shareholders should ensure that the board members nominated by them agree on a specific amount and ask the shareholders to provide the funds, and that, based on this request, the shareholders would conclude a loan agreement. The first-degree and the appellate court both agreed that decisions on the manner of financing the company's operation concern the management of the company business activity and therefore fall within business management. Under the law, shareholders are not allowed to give instructions to the company's board of directors as regards its business management; therefore, both courts held that the respective provision of the shareholder agreement was invalid.

Nevertheless, the SC stated that a distinction should be made between a company's business management and its strategic management. Both business management and strategic management are within the powers of the board of directors of a joint stock company, unless entrusted to another body by law or the company's statutes.
A decision on how (in what manner) the funding of the company shall be secured may or may not fall within business management: securing funds for the day-to-day operation of a company's business is "organising and managing a company's normal business activities"; therefore, it falls under the company's business management. However, in some cases, the issue of securing funds may go beyond normal business management, e.g. when it concerns the financing of significant new projects. If the decision is more of a strategic or investment nature, it falls within the strategic management of the company, which is also within the powers of the board of directors, but the general meeting may, within the limits of the law and the statutes, give instructions to the board of directors. Unless the statutes provide otherwise, the general meeting is allowed to give instructions to the board of directors regarding the company's strategic management. (Please note, however, that shareholders themselves cannot do so, not even to the members of the board of directors nominated by them).

The Supreme Court also dealt with the rules of interpreting a SHA, noting that the principle of autonomy of the parties' will shall apply, therefore an agreement shall be viewed as valid rather than invalid, and priority shall be given to an interpretation that does not result in its invalidity, if such an interpretation is possible. The Supreme Court also noted that if a SHA were to obligate shareholders to give instructions to the board members interfering with business management and to ensure that the instructions are followed by the board even if in breach of their

fiduciary duty (duty to act with due managerial care), such an agreement would be invalid on the grounds of being contrary to law. However, it is possible for shareholders to undertake in a SHA to induce members of the board of directors to be in favour of a certain solution to a matter or to achieve a certain result. Still, it is necessary to respect the condition that while acting to achieve this outcome, the board members must not breach their due managerial care.

We consider this Supreme Court decision very beneficial, both for business operations and transactional practice.

Practical implications of the Supreme Court's decision on determining the scope of business

Corporate law has been shaken up by Supreme Court Decision No. 27 Cdo 3549/2020 on the nullity of a corporation's founding acts stipulating "production, trade and services not specified in Appendices 1 to 3 of the Trade Licensing Act" as its scope of business. Corporations whose memorandums of association or statutes define their business activity in this manner must change their founding deeds and update information disclosed in the Commercial Register.

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According to the Supreme Court, a corporation's business activity defined as "production, trade and services not specified in Appendices 1 to 3 of the Trade Licensing Act" (i.e. as an unqualified trade) is too unspecific, as it does not provide a sufficient picture of what business the corporation is actually engaged in. As a result, such a legal act is null and should not be taken into account.

This type of business activity has been quite common and standard in previous years and both notaries and courts keeping registers have recorded it without any problems. Corporations often took advantage of this flexibility, as the unqualified trade category covers a total of 82 types of trades not requiring special qualification. Consequently, there are currently many corporations with illusive business activities recorded in their founding deeds and commercial registers. These corporations must change their founding deeds, define their business in a clear and specific manner, and change the data disclosed in the commercial register. They may do so, for example, by describing in detail the scope of their business or include one of the types of unqualified trade in their founding acts.

If corporations fail to do so, the court keeping the register may call on them to rectify the situation. If a corporation does not make amends despite the call, the court may impose a penalty of up to CZK 100 thousand or even decide on its dissolution and liquidation.

We are of the opinion that having an unqualified trade recorded as business activity is not in itself an obstacle to conducting business. However, we strongly recommend that the concerned companies change the definition of their business in compliance with the Supreme Court's decision. Since the change of a business activity represents a change of a founding act requiring a notarial deed for limited liability companies and joint stock companies, this change will be associated with additional expenses and administrative burden.

Case law

Mere rental of real property not a VAT fixed establishment

In case C-931/19 Titanium, the Court of Justice of the European Union (CJEU) ruled against the existence of a fixed establishment for VAT purposes solely on the grounds of renting real property without the presence of staff in the country where the rented property is located.

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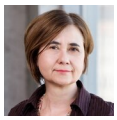
Titanium, a company with registered office on the Island of Jersey that manages real estate, apartments and accommodation facilities, owned real property in Vienna and further rented it to Austrian business entities. Rentals of the properties constituted Titanium's only activity in Austria, and they appointed an Austrian real estate management company to act as an intermediary vis-à-vis suppliers, keep business records, and carry out all administrative activities. Titanium retained all important decisions as regards renting the real property, such as entering into and terminating leases, arranging for repairs of the real property, etc.

The Austrian tax administrator was of the opinion that under Austrian legislation, the lease of immovable property located in Austria gives rise to a fixed establishment for VAT purposes, and, accordingly, Titanium was to pay VAT on its rental income in Austria. The question before the court was whether a fixed establishment must always involve human and technical resources or whether, in the specific case of renting real property, the real property itself could be regarded as a fixed establishment even without staff (human resources) of its own.

In the CJEU's opinion, and in line with established case law, the concept of a fixed establishment requires the presence of both human and technical resources that would enable it to independently provide the services in question. In other words, the real property that has no human resources available through which it could act independently does not meet the criteria laid down in the case law for it to be classified as a fixed establishment for VAT purposes. In line with these conclusions, the CJEU held that if Titanium does not have its own staff through which they would rent the property, then the property cannot constitute a fixed establishment for VAT purposes.

News in brief, July 2021

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



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DOMESTIC NEWS IN BRIEF

- On 28 June 2021, the government extended the duration of Regime A of the Antivirus programme concerning employers whose employees are ordered into quarantine or isolation due to COVID-19 until the end of October 2021.
- Effective from 24 June 2021, the CNB Bank Board increased interest rates, in particular the two-week repo rate used by the financial administration to calculate default interest, to 0.50%. The existing rate of 0.25% was in effect from 11 May 2020 to 23 June 2021. The two-week repo rate of 0.25% is to be used to calculate default interest for the first half of 2021 and the second half of 2020, and the current repo rate of 0.50% shall apply for the second half of 2021.
- In connection with the declaration of a state of emergency in the Břeclav and Hodonín regions, the Ministry of Finance has prepared a tax relief package. The general tax pardon published in the ministry's official Financial Bulletin covers the following:
    - postponement of personal and corporate income tax due date from the end of June until the end of August
    - postponement of deadlines for filing tax returns and VAT ledger statements and paying VAT for May, June and the second quarter of 2021 until 25 August 2021
    - waiver of penalties for VAT ledger statements filed from 25 June 2021 to 31 July 2021
    - waiver of road tax prepayments payable on 15 July
    - waiver of income tax arising on the provision of subsidies and loans from the State Fund to Support the Redevelopment of Tornado-Destroyed Housings.
- GFD Instruction D – 50, determining the format and the structure of data messages, was published in Financial Bulletin No. 24/2021.
- The financial and customs administrations have published their Report on Activities for 2020, containing information about the collection of taxes, the Ministry of Finance's legislative activities, and inspection activities.
- The Senate has referred back to the Chamber of Deputies a draft amendment to the Act on State Social Aid (Print 1 116), also including an amendment to the Act on Income Tax cancelling the tax bonus amount limit of CZK 5,025 a month and increasing tax credit per second, third and any subsequent children. The Senate proposes changing the annual tax credit amounts to be dividable by twelve (from CZK 22,315 to CZK 22,320 and from CZK 27,835 to CZK 27,840) while also amending the amendment's effectiveness. Deputies may either pass their version or the version proposed by the Senate, or they may decide not to approve it at all. The amendment is planned to be debated at the deputies' session in July.

FOREIGN NEWS IN BRIEF

- The OECD has published comments emanating from public consultations on the proposed changes to the Commentaries in the OECD Model Tax Convention with respect to Article 9 regulating the tax treatment of transactions between related parties. The most discussed change is the inability to apply the mutual

agreement procedure (under which a mutual agreement on taxation between contracting states is applied) where tax on a transaction between related parties is additionally assessed based exclusively on national legislation (e.g. non-deductible expense) and not on challenging the arm's length principle upon which the price between related parties was determined.

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