



COMPREHENSIVE LEGAL, TAX,
ACCOUNTING AND AUDIT SERVICES

- ▷ Amendments to Value Added Tax Act
- ▷ Amendment to Income Tax Act 2019
- ▷ Planned amendment to Electronic Records of Sales Act (EET)
- ▷ Register of true owners

AMENDMENTS TO VALUE ADDED TAX ACT

Currently, two amendments to the Value Added Tax Act are under preparation. The first amendment reflects changes made in the area of electronic records of sales (the “EET”) and the second one will be introduced as a part of the tax package. It is possible that both amendments will be significantly modified in the legislative process. We will inform you of any such changes in due time.

Changes to rates

Following an amendment to the EET Act, with the effect from 1 January 2019, VAT rates will be reduced to 10 % for the following goods and services - processing and distribution of water through water supply networks, drainage and treatment of sewage, restaurant and catering services (with the exception of sale of alcoholic beverages or tobacco products; however, beer tapped from containers larger than 10 litres will also be taxed by the reduced 10% VAT rate), hairdresser, cosmetic and similar services and sale of cut flowers.

Vouchers for goods and services

In compliance with a European Directive, the VAT Act will redefine single-purpose and multipurpose vouchers used for sale of goods and services. Rules applying to single-purpose vouchers will be similar with rules applying to delivery of goods and provision of services, which means that VAT will be paid already upon the voucher being issued. On the other hand, multipurpose vouchers will not be subject to taxation and VAT payment until the moment of the goods or services paid for by the voucher are supplied.

VAT correction in case of receivables outstanding

The amendment significantly extends the number of situations in which VAT payers may claim return of VAT paid on issued invoices from the state. Currently, VAT payers may claim return of VAT only in case of the debtor’s bankruptcy and when several other rather strict

conditions are met. From now on, the correction of tax on output will, in certain circumstances, be possible even in the event the creditor has unsuccessfully tried to enforce the debt in enforcement proceedings, and in the event of dissolution of the debtor with liquidation or in the event of the debtor’s death.

Services provided electronically

Under the current legislation, providers of digital services are obliged to follow VAT regulation and pay VAT applicable in states in which its customers (non-taxable legal entities and non-taxable natural persons) are located. This will now change as the amendment introduces an annual threshold of EUR 10,000 up to which it will be possible to follow regulation applicable in the country where the provider is established. In practice, this means that Czech VAT payers providing digital services to other countries only up to a certain limit will be able to apply Czech VAT rate of 21% and will not fall under the special mini one stop shop regime (MOSS).

AMENDMENTS TO VALUE ADDED TAX ACT

VAT on hire purchase

Under the current legislation, payment of the entire VAT at the beginning of a hire purchase is required only in case of hire purchase contracts in which the lessee's obligation to purchase the hired property is declared at the very beginning of the hire purchase. According to the amendment, the duty to pay VAT at the beginning of the hire purchase will be extended to contracts which provide the lessee with an option to purchase the property if, considering all circumstances, it is clear from the beginning of the contract that the lessee will use this option.

Corrections of tax deductions in case of repairs of real estate

The amendment introduces a duty to correct the original VAT deduction in case of any repair of real estate exceeding CZK 200,000 excl. tax, if, within 10 years from the repair of the real estate, the real estate is sold.

Other changes

In addition to the main changes specified above, the amendment introduces a number of technical changes:

- ▶ For services provided in connection with lease of real estate, the date of the respective taxable performance will be the date on which the actual amount which should be re-invoiced to the lessee is ascertained.
- ▶ From now on, it will be possible to issue a single summary tax document covering both the receipt of the advance payment and the final settlement if the advance payment is received and the taxable supply is effective within one calendar month.
- ▶ The special coefficient rounded to 4 decimal places will no longer be used to calculate VAT from payments incl. tax ("from gross amount" calculation), which means that there will no longer be any difference from VAT being calculated from payments excl. tax („from net amount" calculation).

- ▶ From 2020, it will no longer be possible to voluntarily charge VAT on lease of family homes, residential premises and flats.
- ▶ When registering for VAT, it will be possible to claim VAT deductions for individual invoices issued for purchase of property (classified as property used by the taxable person) made up to 12 months prior to the registration, even if the individual partial supplies were made up to 60 months prior to registration.
- ▶ The deadline for filing an additional tax return form will be the end of the respective month if the reasons for filing the additional tax return form have been ascertained before the 15th day of the given month.
- ▶ From 2020, „identified persons" will also be obliged to file their VAT return forms electronically.



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AMENDMENT TO INCOME TAX ACT 2019

An amendment to the Income Tax Act is currently in the consultation phase of the legislative process. The main focus of the amendment is the implementation of the European Anti Tax Avoidance Directive (ATAD) in the area of corporate income tax. The amendment introduces rules for limitation of deductibility of interests and for exit taxation, rules against the abuse of tax regimes and rules applying to controlled foreign entities and hybrid mismatches. All these changes will apply only to legal entities which are subject to corporate income tax in one or more member states of the European Union, including permanent establishments of foreign (non-EU) tax payers if such establishments are located in one or more EU member states.

Limitation of deductibility of borrowing costs

The declared goal of the proposed legislation

is to prevent artificial decreasing of tax base by debt financing costs. Excessive borrowing costs (the difference between tax deductible borrowing costs and taxable interest revenues) will be deductible only up to a certain limit.

Should the excessive borrowing costs exceed said limit, the tax payer concerned will be obliged to increase its economic results by this amount. The limit for tax deductibility is either 30% of earnings before interests, taxes, depreciation and amortization or CZK 80 million, depending on which of these amounts is higher.

The limitation of deductibility of exceeding borrowing costs applies to all corporate income tax payers. The Czech Republic however used the opportunity granted by the Directive to exempt financial institutions and persons which are not a part of a group from these rules.



AMENDMENT TO INCOME TAX ACT 2019

As tax payers with excessive borrowing costs only in certain limited periods (e.g. due to large scale investment) could be disadvantaged by the new regulation, they will be able to decrease their economic results in the following taxation periods by the amount by which, pursuant to the new regulation, their economic results increased in one year, on condition that in the following taxation periods the excessive borrowing costs have not reached the stated limit.

Please note that the current regulation of tax deductibility of interests, such as the thin capitalisation test and the condition of paid interests if the creditor is an individual who does not keep accounting records, remains unaffected. As the first step, the tax payer will ascertain the amount of deductible interests. The next step will be to take the excessive borrowing costs test.

Taxation in case of relocation of assets abroad

With the effect from 2020, cross-border relocation of assets by a corporate income tax payer from the Czech Republic abroad without the change of ownership will be subject to taxation.

Although there will be no actual sale of property, the Czech Republic introduces a fiction of sale of property in order to keep the right to tax revenues from the subsequent paid transfer of assets relocated abroad. Relocation of assets from the Czech Republic abroad will be considered a sale to itself for an open market value. The tax payer will therefore be obliged to tax the fictional revenues made from the relocation. The tax payer will however have an option to deduct the net book value of the assets relocated.

Taxation due to relocation without change of ownership will apply to the following cases:

- ▷ A legal entity, tax resident in the Czech Republic, relocates assets from the Czech Republic to a permanent establishment abroad and revenues from a subsequent sale of this property will be exempted from taxation in the Czech Republic.
- ▷ Transfer of assets from a permanent establishment in the Czech Republic abroad, if the Czech Republic has no right to tax revenues from a subsequent sale of the property.
- ▷ The tax residency of the tax payer changes and consequently, the Czech Republic has no right to tax a subsequent sale of the assets relocated.

It will be possible to spread the payment of the tax on relocation of assets into 5 years, if assets are transferred without a change of ownership within the European Union or the European Economic Area.

AMENDMENT TO INCOME TAX ACT 2019

Controlled foreign companies

Rules applying to controlled foreign entities are based on the principle that a corporate income tax payer who is a tax resident in a given state shall include passive income and income from artificial transactions made by a foreign entity controlled by the tax payer in its tax base, if the controlled entity's tax burden is lower than one half of the tax the entity would be obliged to pay if it was a tax resident in the controlling tax payer's state.

The amendment to the Income Tax Act provides an exhaustive list of examples of passive income which is subject to this rule. Examples include licence fees, shares in profits, borrowing revenues, revenues from the sale of goods and provision of services bought from affiliated persons without any added economic value or with a limited added economic value, revenues from a transfer of shares in a company etc.

The aim of the proposed regulation is to prevent the avoidance of tax obligations of corporate income tax payers who are tax residents in the Czech Republic and establish subsidiaries or permanent establishments in low tax jurisdictions in order to intentionally divert revenues from the Czech Republic.

Revenues made by Czech tax residents' foreign subsidiaries or their permanent establishments are generally not subject to taxation in the Czech Republic, unless they arise out of sources in the territory of the Czech Republic. By introducing a legal fiction that activities carried out by such controlled entities are carried out directly by their parent companies or headquarters (controlling entities), the revenues made by such controlled entities will be included in the controlling entities' tax bases and taxed in the Czech Republic.



AMENDMENT TO INCOME TAX ACT 2019

It is necessary to note that this legal fiction will apply only if two conditions are met at the same time. The first condition is that the controlled foreign entity's tax obligation in its domestic state is lower than one half of the tax which the entity would be obliged to pay if the foreign entity were a Czech tax resident. The second condition is that the controlled foreign entity does not carry out significant economic activities.

Hybrid mismatches

The legislation of the Czech Republic will with the effect from 2020 transpose regulation introduced by the ATAD Directive concerning hybrid mismatches. Hybrid mismatches are cases concerning corporate income tax payers which lead to mismatching results, i.e. double deduction (costs may be deducted by several companies without the corresponding revenues being included in the tax base) or deduction without any corresponding revenue on the part of another company.

Hybrid mismatches arise in situations in which in different countries, transactions are assessed differently from the tax perspective. The amendment to the Income Tax Act introduces an obligation to subject such hybrid mismatches appearing between affiliated persons to additional taxation.



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PLANNED AMENDMENT TO ELECTRONIC RECORDS OF SALES ACT (EET)

Following a decision of the Constitutional Court no. 8/2018 Coll. from December 2017, which abolished certain parts of the EET Act (for more details, please see our newsletter from February 2018), the Ministry of Finance initiated in the middle of March 2018 an external consultation process concerning a draft amendment to the EET Act. Apart from reflecting requirements of said decision of the Constitutional Court, the amendment introduces other more general conceptual changes.

The amendment's aim is to introduce the following major changes to the system of EET:

- ▶ The 3rd and 4th phases of EET should start at the same time – from the third month following the amendment becoming effective (expected 1 March 2019).
- ▶ Payments made by debit and credit cards will no longer be subject to EET.

- ▶ The scope of services which are not subject to the EET will be extended (telecommunication and other services provided through a public mobile phone network which represent the use or clearing of another payment (made by a pre-paid card), revenues from gambling, revenues from commercial air transportation or revenues made by severely visually impaired individuals).

- ▶ Introduction of a special off-line regime for small businesses – self-employed entrepreneurs (i) who are not VAT payers, (ii) who have maximum one employee, (iii) whose registered sales have not exceeded CZK 200.000 in twelve consecutive months; and (iv) who have not received more than 1.000 recorded payments in twelve consecutive months. Paper receipt forms will be distributed by the Financial Administration.

- ▶ The obligation to record sales will apply only to payments received in the territory of the Czech Republic.
- ▶ Reintroduction of the obligation to state tax identification numbers on the receipts, unless the tax identification number contains the taxable person's birth number.



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REGISTER OF TRUE OWNERS

From 1 January 2019, all companies will be obliged to register their true owner(s). Information on the true owners will be registered in the non-public section of the Commercial Register (or in the non-public section of another public register, if applicable), and will not be publicly accessible. The true owners should be registered during the course of 2018 so that before 1 January 2019, the registration is complete. Until 1 January 2019, the registration of true owners is relieved from court fees. Please note that an obligation to internally identify the true owners of a company already applies today.

Who is the true owner?

The true owner is always a natural person who, whether de facto or de iure, is able to wield a decisive influence over the respective

entity. In a commercial company such a person is defined as someone who

- ▷ whether alone or together with other persons (acting in concert), holds more than 25 % of voting rights in the entity or its share in the registered capital of the company is more than 25 %;
- ▷ controls alone or together with others (acting in concert) the commercial company defined in point 1;
- ▷ is supposed to be the recipient of at least 25 % of the company's profits;
- ▷ is a member of the governing body or a representative of the governing body of the company if the true owner does not exist or cannot be found.



REGISTER OF TRUE OWNERS

For other legal entities (such as foundations, institutions, trust funds, associations or associations of unit owners), the law sets less stringent criteria, and the time limit for registration of the true owners is extended to 1 January 2021.

Liability for registration of true owners

The governing body bears liability for registration of the true owners, regardless of how difficult it is to find the true owners. If the true owners cannot be found, the governing body has an obligation to register itself as the true owner. This may potentially lead to more strict checks of these persons for example in banking transactions, due to the provisions of the Act on Prevention of Legalization of Proceeds of Crime. In such cases, it is recommended

to have sufficient documents available attesting to the fact that the true owners do not exist or is not objectively possible to trace them. We strongly recommend that this duty shall not be underestimated and that especially in unambiguous cases, identification of the true owners shall be commenced as soon as possible.



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