BDO NEWS

MAY 2020 - ISSUE 5

WWW.BDO.CZ

LONG-TERM INVESTMENT ACCOUNT AS AN ALTERNATIVE TO RETIREMENT SAVINGS
PAGE 2

VAT – RATE AMENDMENT
PAGE 3

AN OVERVIEW OF THE MOST IMPORTANT TAX AMENDMENTS
PAGE 4

EDITORIAL

Dear Readers
Life is beginning to return to normal, factories are starting up their production lines, and people are once again returning to shops and offices.
But despite the seemingly positive developments, we should remain vigilant. Unfortunately, even for healthy businesses, there may be a major drop in revenues and liquidity that cannot be managed without early intervention in the form of restructuring or insolvency proceedings. Moreover, I believe that COVID-19 has not only accelerated structural changes in the way services are produced and provided but will also lead to a change in the way they are taxed.
Right now, think about the situation of your company, remember your responsibilities and the duty of due managerial care. Consider taking steps that not only ensure the continuity of the company, but also protect the owner's assets. Unfortunately, by no fault of their own, the situation can develop critically, and we should proceed in accordance with the law. If you perceive any danger, you need to act immediately, either to set aside the company's most valuable assets and move them to a safe deposit box without additional taxation, or to have an analysis carried out, for example, to see if you are obliged to file for insolvency. Otherwise, you may also find that you are indefinitely liable for everything as an individual and you could possibly commit a crime. Once the liabilities outweigh the assets at market value, it is too late.
However, if you are a dependent subsidiary of a foreign group (dependent manufacturer or retailer), make sure that the group still expects your fair profit to be secured.
Although the severe economic recession does not change international transfer pricing rules, it is still the case that for a "wage labour" producer, production cannot be sold at a loss. Most of us would also not pay to go to work.
As I mentioned in the introduction, the operation of companies and the state is beginning to return to normal, so in this issue we have prepared an up-to-date overview of already approved and planned news in the area of tax.
Please also keep in mind that we regularly update all important information regarding government actions or financial assistance related to COVID-19 on our website.
I wish you much fortitude and good news!

Martin Houska
Partner

CONTENT

BDO CZECH REPUBLIC

- Audit, Tax, Accounting & Payroll Advisory, IT and Valuation
- 450 specialists
- 35 Certified Tax Advisers, 30 Certified Auditors, 5 Certified Appraisers
- 6 offices in the Czech Republic

LONG-TERM INVESTMENT ACCOUNT AS AN ALTERNATIVE TO RETIREMENT SAVINGS

Last year, the Government of the Czech Republic presented the Concept of Development of the Czech Capital Market with the aim of increasing its competitiveness. The intention is to motivate higher use of the capital market in comparison to the money market and to reduce the outflow of investment abroad. The General Directorate of Finance proposed a draft law which is expected to be effective from 1 January 2022. One of the target groups for the concept is households and their long-term savings.

The legislature's intention is to **increase household savings**, the possibility of a **better appreciation** of these savings and a partial transfer of funds to the capital market. It is clear from practice that tax benefits for long-term financial products are an important motivation for their use. Therefore, it seems logical for the legislator to presume that **extending the relevant tax advantages** will lead to the fulfilment of its intentions.
The new tax-supported product should be the so-called **long-term investment account**. Its purpose is to create retirement savings through investments in stocks, bonds or investment funds. It should be a more dynamic alternative to traditional products, which often do not even cover inflation. The long-term investment account should be in the form of a „personal savings account" widely used in developed capital markets such as the US or the UK.
At the same time, the amendment simplifies the overly complicated construction of tax laws governing this area, in particular by introducing the legislative acronym „**tax-supported retirement product**" and by providing an overview of the necessary conditions for the tax benefits for products in one place. At the same time, the existing limits for deduction from the tax base to CZK 48,000 per year are merged, which should allow taxpayers greater flexibility in choosing an investment strategy.

Tax benefits	Current status	Draft law
Deduction from personal income tax base	Max. CZK 24,000 to pension funds and max. CZK 24,000 to life insurance	Max. CZK 48,000, extension of supported products by long-term investment account
Exemption of employer's contribution from personal income tax	Max. CZK 50 000	Max. CZK 50,000, extension of supported products by long-term investment account
Possible tax deductibility of cargo in the form of employer contribution	Without restriction	Without restriction

Contributions in favour of financial products for retirement savings are a popular benefit for employees due to their tax advantages. If you plan to update the company's benefits policy in a forward-looking way, we recommend that you also remember the new long-term investment account. If the relevant institutions offer the long-term investment account product, the draft law might bring a positive impetus to the amount people save and help them achieve greater flexibility in their long-term investment strategy.
We will keep you posted on further developments.

Monika Lodrová
monika.lodrova@bdo.cz

VAT – RATE AMENDMENT

New VAT rates apply to selected services from 1 May 2020. Services that now fall under the lowest tax rate (10%) can be divided into three categories: (i) catering services; (ii) services with a high proportion of human labour; and (iii) other services.

The **first category** - catering services - is the most discussed one. From 1 May 2020, it is necessary to correctly assess whether this is really a catering service for which the taxpayer can apply a 10% VAT rate. If the payer concludes that it cannot, the VAT rate will remain at 15%, and in the case of draft alcoholic beer at 21%.
To be a catering service at the 10% VAT rate, additional services must be provided at the same time. Services that can be considered additional include, for example, providing a dedicated place with tables and chairs to consume meals or providing toilets and washable utensils. The rule here is that the more additional services, the better.
The same condition applies to the serving of non-alcoholic drinks and draft alcoholic beer. The information provided by the General Directorate of Finance does not exclude the possibility of applying a 10% VAT rate to catering services and the sale of food produced by a third party, in cases where the condition of additional services is met. However, in these cases, I recommend increased caution.
On the other hand, this information completely excludes the application of a 10% VAT rate for food that can be consumed on the spot (e.g. a hot dog), but without the provision of related ancillary services, in which case it is a supply of goods and not a catering service. The same applies to goods primarily intended to be taken with you (e.g. packaged food, pizza in a box), regardless of the amount of additional services.

The **second category** includes:

- Interior cleaning services - performed in households.
- Window cleaning services - performed in households.
- Home care for children, the elderly, the sick and the disabled.
- Repair of footwear and leather goods.
- Bicycle repair.

- Hairdressing and barber services.

The **third category** includes:

- Potable tap water. Potable water distributed in another way is subject to a 15% VAT rate. The information provided by the General Directorate of Finance specifies that the 10% VAT rate will also apply to hot water which was made from potable tap water.
- Water treatment and distribution networks.
- Drainage and wastewater treatment, including other services related to these activities.
- Electronically provided publications, which thus reach the level of the printed ones. Simply put, the 10% VAT rate is applied to the kind of electronic service (publication) where a 10% VAT rate would have been applied if the publication had been delivered in printed form.
- Colouring books, maps.
- Book lending.

I would like to point out that in order to apply any reduced rate of VAT, the transaction must be correctly classified, while meeting the verbal description given in the relevant annexes to the VAT Act.
In conclusion, apart from the catering services issues, the rate amendment is well arranged. The welcome news is that VAT will be reduced for businesses which provide the above-mentioned services. For the goods or services concerned, lowering rates may even mean a slightly cheaper price. However, in my experience, I believe this will not happen and that there will be no more than a temporary stagnation of these prices.

Petr Linx
petr.linx@bdo.cz

BDO BRINGS ABOUT THE END OF INTERMINABLE TAX AUDITS, SUPREME ADMINISTRATIVE COURT REFUSES TO CHAIN TAX LOSSES

In its judgment of 13 May 2020, the Supreme Administrative Court (SAC) rejected the previous years of practice by tax authorities as regards the so-called chaining of tax losses. A team of legal and tax specialists from BDO, led by Lenka Lopatová, Vít Křivánek and Jiří Šmatlák, challenged the current practice and the SAC agreed with them.

The Financial Administration illegally exceeded the length of tax audits, which normally should not go beyond three years in one loss-making year. This practice not only led to a high administrative burden for businesses, but ultimately extended the audit period practically „indefinitely". In practice, it was not unusual for the tax administrator to audit a business's tax obligations going as far back as 10 years.
Thanks to the judgment of the SAC, the established procedure of tax administrators is fundamentally changing. Businesses have now been assured that the tax administrator cannot require a longer audit period than stipulated by law. In addition, all businesses for which the tax administrator has been carrying out a tax audit for years with reference to so-called chaining losses have the opportunity to effectively defend themselves against this illegal practice.

What exactly was the dispute about?
In its judgment, the SAC dealt with the case of a domestic company that in 2008 and 2009 reported losses which it applied in its tax returns in subsequent tax periods in accordance with the Income Tax Act.
The question at issue between the taxpayer and the tax administrator (hence the Regional Court) was whether the loss-making year 2009 or its deadline in which the tax administrator is entitled to audit the tax also affects the loss-making year 2008 or its deadline (by using the principle of so-called chaining of losses).
As stated in Section 38r (2) of the Income Tax Act, the deadline for determining tax for the tax period in which the tax loss arose, as well as the deadline for determining tax for the following five tax periods in which this loss can be claimed, expires simultaneously with the deadline for the last tax period in which the loss can be claimed.
In the case under review, the deadline for 2008 expired at the same time as the deadline for the tax period from 1 April 2013 to 31 March 2014 (financial year). The same rule applies to the loss for 2009 - in this case, the last (reference) tax period was 2015.
Note that the **2009 tax period** is, on the one hand, **the year in which the loss occurred**, and thus the first year determining the tax assessment deadline for this and the following five tax periods, but **also the tax period in which the loss for 2008 can be claimed for the first time**. The year 2009 therefore finds itself in a dual position.
The Financial Administration has long and consistently adhered to the interpretation of the **so-called chaining of losses**, i.e. a state, in light of the case under consideration, in which **the 2009 tax loss directly affects the course of the 2008 deadline** due to the dual position of 2009 indicated above. One of the consequences of this legal opinion could be an **infinitely long deadline** for carrying out a tax audit (if, for example, the taxable person declares a tax loss every fourth tax period).
The SAC heard our objections - according to it, from several possible interpretations of the provision of the Income Tax Act in question, it is necessary to clearly give priority to the one **that completely prohibits the possibility of chaining**. Another application would not respect the meaning of the legal standard in question and, above all, would **disproportionately interfere with the legal certainty of taxpayers**.
According to the court, an interpretation admitting the so-called chaining of losses does not even have explicit support in the text of the law itself and represents only an inadmissibly expanding interpretation of the given provision.
As the SAC points out, the purpose of clearly setting the deadline for tax assessment and its preclusive nature is on the one hand to ensure legal certainty both on the part of taxpayers and the tax administrator,

but also to create an incentive for the timely organisation of legal relations between the two parties. At the same time, this deadline represents a certain barrier to possible arbitrary interventions in the legal sphere of taxpayers, which could occur in its absence. We can reasonably assume that this appeal of the court is a clear reference in the proceedings under consideration to the laconic, passive and thus uneconomical and inefficient approach of the tax administrator, which audited the tax liability for the 2008 tax period more than 10 years after the end of this tax period.

What does the court decision mean for further practice?
First, it is finally not necessary to worry about tax audits in the order of five years or more with reference to the principle of so-called chaining of losses. Following the court's decision, the **tax administrator is limited to a standard length of a maximum of three years**.
In conjunction, the chances of successfully defending tax claims before the tax administrator therefore increase, as it will not be necessary to prove facts, for example, up to 10 years or more old. The court's opinion should also help make tax proceedings faster and more efficient, as the tax administrator will no longer be able to legitimately demand „extended" deadlines for carrying out tax audits with reference to the principle of so-called chaining of tax losses. Finally, the court ruling showed that justice in taxes still exists.

Lenka Lopatová, Vít Křivánek, Jiří Šmatlák
lenka.lopatova@bdo.cz, vit.krivanek@bdo.cz, jiri@smatlak.cz

AN OVERVIEW OF THE MOST IMPORTANT TAX AMENDMENTS: TAX REGULATIONS

The draft of an extensive amendment to the Tax Code, which the Senate returned to the Chamber of Deputies with amendments, was not approved on 22 April 2020 in either the Senate or the Chamber of Deputies. The whole long-prepared amendment thus fell under the table.

The unapproved amendment also included a prestigious project of the Ministry of Finance for the electronic taxation of MY taxes, a significant revision of the sanction system (interest and fines) or the possibility of an advance on the undisputed part of the excessive deduction. Therefore, on 27 April 2020, the Government of the Czech Republic approved another amendment to the Tax Code, which takes over a number of provisions of the rejected amendment:

- extensive modernisation, simplification and electronisation of taxes, including the establishment of the so-called online tax office (MY Taxes project);
- for taxable persons who submit tax returns electronically, the deadline for submitting income tax returns will be extended by one month;
- simplification of control procedures;
- revision of the sanction system;
- partial refund of excessive VAT deductions in the form of advances already during the control procedure;
- maintaining a tolerance period of five working days for late submission of tax returns.

The new government proposal introduces:

- the possibility of an individual waiver of a fine for late tax claim, which is not possible today;
- double interest on incorrectly secured or recovered tax if it is unjustifiably recovered from taxable persons in the context of a seizure;
- a tolerance period during which interest on arrears does not accrue; it should have been deleted in the rejected amendment, it is now proposed at three calendar days (currently four working days apply);
- the format of the so-called form submissions will be determined by a decree of the Ministry of Finance;
- the deletion of the original extension of the deadline for returning the excess deduction from 30 to 45 days (remaining 30 days).

The effectiveness of the government's tax code amendment is proposed for 1 January 2021 and according to the proposed transitional regulations, it would be possible to use a one-month extension of the deadline for filing electronic income tax returns for tax returns filed for 2020.

Jiří Čermak
jiri.cermak@bdo.cz

AN OVERVIEW OF THE MOST IMPORTANT TAX AMENDMENTS: INCOME TAX ACT

The Ministry of Finance introduced an amendment which should affect selected provisions of the Income Tax Act with effect from 2021. Among the most important changes proposed are:

- extension of the time test liberation of revenue from real estate, from the current five years to 15 years;
- introduction of meal allowance in cash as an option, which would be a tax expense on the part of the employer without restriction; for employees it would be exempt income of up to 70% of the meal allowance;
- abolition of the exemption for interest income from bonds issued by Czech companies or the Czech Republic to non-residents of the Czech Republic; this income would be subject to withholding tax;
- change in the taxation of bond income - the subject of the tax will no longer be the difference between the nominal value of the bond paid upon its redemption and the issue price, but the difference between the nominal value and the acquisition price of the bond. In addition, this income will no longer be subject to withholding tax, but will be taxed under the sub-tax base as income from capital assets;
- change in the frequency of reporting of exempt income flowing abroad, once per calendar year, with a deadline of the end of January of the following year (instead of the current monthly reporting if the obligation arose in a given month);
- increase of the limit on the obligation to report exempt income paid abroad, from the current CZK 100,000 to CZK 300,000;
- definition of jurisdictions that do not cooperate in tax matters, with all revenues of controlled companies from this list being included in the tax base of the Czech controlling company.

Even though lately tax legislation has been becoming stricter, the suggested changes relating to income paid abroad would mean a significant administrative relief.
The amendment is now in the comment phase and I expect a number of changes, which we will inform you on in our newsletter.

Lenka Froschová
lenka.froschova@bdo.cz