TAX FRESH

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Dear Business Friends,

Let us present the latest tax updates in our Tax Fresh bulletin. Recent decisions of many companies to invest substantial amounts of money in research and development inspired us to include information on the prepared amendment to the relevant law. Also, we would like to highlight the new Act on Electronic Reporting of Sales and the changes regarding the immovable property acquisition tax. We also include a very useful VAT tool – a chart showing current VAT rates in all EU countries plus Switzerland and Norway.

In addition, we would like to share our joy over the fact that in this year's strong competition, it was our partner who received the "Tax Star of the Year" award. We hope we will have the opportunity to celebrate our 25th anniversary together - not only with work.

Yours faithfully,

Šárka Adámková
Tax partner

Ladislav Dědeček
Tax partner

HLB PROXY
Audit & Tax Services

PERSONAL INCOME TAX
- INCREASE IN CHILD TAX CREDIT

Please note the change valid as of May 2016. Act no. 125/2016 Coll. of 25 April 2016 amends the Income Tax Act, increasing the Child Tax Credit for the second child from CZK 15,804 to CZK 17 004 per annum, and for the third and every next child from CZK 17,004 to CZK 20,604 per annum.

The law entered into force on the first day of the calendar month following the act publication date, i.e. on 1 May 2016.

The General Financial Directorate's Statement stipulates that employers should first subtract the tax credit from taxes of their employees who claim the child tax credit in **May 2016**.

The monthly amount of the tax credit is CZK 1,417 for the second child and CZK 1,717 for every next child. The remaining part of the tax credit for the period January – April 2016 shall be accounted for in the annual settlement of taxes or in the personal income tax return for 2016.

The tax credit for the first child remains the same, i.e. CZK 13,404 per year, which corresponds to CZK 1,117 per month. We have been informed that another amendment is currently being prepared which should increase the credit for the second and every next child as of 2017.

CORPORATE INCOME TAX
- RESEARCH AND DEVELOPMENT DEDUCTION

An increasing number of companies focuses on research and development. This trend is reflected in the draft of Amendment no. 489/0 to Act no. 130/2002 Coll. on support of research and development from public funds. The amendment is currently being prepared by the government and should expand the scope of deductible items related to research and development.

Deduction in Practice

The corporate deduction applicable under the Income Tax Act in the Czech Republic, under the stipulated conditions, is as follows:

- ✓ **100% of the expenses** on research and development spent within the relevant tax period
- ✓ **plus 10%** of the expenses exceeding the amount of expenses spent within the preceding tax period, i.e. 110% of the annual increment.

The deduction is used by the state to reward companies that take interest and invest in research and development. <u>Such companies can deduct their expenses twice – once as ordinary tax deductible expenses, and then again in the form of deduction.</u>

What are the most common expenses eligible for the deduction?

The deduction stretches especially to the related labour costs (including social and health insurance payments), tax depreciation of assets, operating expenses (e.g. related to the acquisition of raw materials, inventories, literature or electricity), etc. The essential condition naturally is that such costs must be directly related to the implementation of a research and development project.

The enticing deduction is controlled by <u>**strict administrative rules and risks**</u> which need to be observed very carefully. One of the essential conditions for using the deduction is the existence of a written document "Research and Development Project" conforming to the legal requirements. The "Project" document must be issued before the work on the project commences. Another very important and tricky condition is that the project must be a genuine research and development project, not only an innovation project. This condition must be closely observed, as tax administrators in the Czech Republic meticulously verify the eligibility of individual projects.

THE ACT ON ELECTRONIC REPORTING OF SALES ENTERED INTO FORCE

The Act on Electronic Reporting of Sales was published in the Collection of Law on 13 April 2016 under no. 112/2016, together with Act no. 113/2016 Coll. which lowers the VAT rate for catering services (excluding alcoholic beverages) from 21 to 15%.

The enactment of the law draws a symbolic curtain over lengthy political disputes and vivid debates about viability and practicability of electronic reporting. It allows entrepreneurs to move on and focus on the preparations for the new obligation.

The obligation for companies and entrepreneurs to record their sales should start as follows:

- from 1 December 2016 – accommodation and catering services;
- from 1 March 2017 – retail and wholesale;
- from 1 March 2018 – other services, professionals, transport, agriculture;
- from 1 June 2018 – selected crafts and production.

To check which category your company falls into, use the NACE code of your activities at:

http://www.e-trzby.cz/cs/odkdy-evidovat-trzby

The obligation to record sales relates to all entrepreneurs who accept payments in relation to their business, whether in cash, by card or another similar method (bank transfers are not included).

The obligation to record sales concerns only payments related to business activities, i.e. not revenues from non-business activities such as rent, as stipulated in Article 9 of the Income Tax Act, or revenues from irregular activities as stipulated in Article 10 of the Income Tax Act (e.g. the sale of garden surpluses).

The law specifies a list of exceptions from the obligation to record sales. For instance, there is a general pardon for banking and financial institutions (banks, insurance companies, bond traders, investment funds, etc.), exceptions based on the source of the revenue (e.g. transactions within employment relations, public transport fares, or vending machine sales).

VAT liability is not a criterion in terms of sales records, the obligation applies to all entrepreneurs, regardless of VAT registration.

Entrepreneurs shall be obliged to:

- ask the tax administrator for authentication data (before the reception of the first recorded payment, but no sooner than on 1 September 2016);
- acquire equipment for electronic reporting of sales (any internet connected device, not necessarily a cash register);
- send the payment data to the tax administrator in real time;
- wait for the transaction code;
- issue a receipt with the specific transaction code. The act does not specify the delivery method or format of the receipt consequently it allows the entrepreneur also to issue an electronic receipt (not printed) and deliver it via email, MMS or bluetooth).

The Act on Electronic Reporting of Sales also specifies the duty of the tax administrator to carry out mystery shopping to verify the fulfilment of the above specified duties of entrepreneurs, especially with respect to recording individual payments and issuing receipts with transaction codes. Failure to fulfil the obligations might lead to a fine of up to CZK 500,000 or even closure of the business (in the case of wilful violation of the law).

For more information about specific obligations relating to the act, please feel free to contact our office.

GRATUITOUS INCOME THROUGH THE EYES OF TAX ADMINISTRATION

For nearly one year, since April 2015, the Czech Chamber of Tax Advisors has had a debate with representatives of tax administration over the tax implications of gratuitous income (contribution addressed to the Coordination Committee registered under no. 452/22.04.15). Although representatives of the General Financial Directorate did not answer all the questions related to the issue, their statement is a valuable tool in settling disputable questions related to gratuitous income.

The most important conclusions for daily accounting:

- Gratuitous services (e.g. painting of office walls, free accounting services) shall be added to tax base by the recipient of the service (recipients will increase their tax base by the value of the received services, in accordance with Article 23, (3)(a), section 16 of the Income Tax Act) and subtracted from tax base at the same time (recipients will decrease their tax base by the same amount, in accordance with Article 23(3)(c), section 8 of the Income Tax Act). This way, the reception of gratuitous services shall have no impact on the tax base. The subtraction from tax base is not an obligation, but a possibility.

  The same process on the part of the recipient is applicable in the case of gratuitous credits and loans, and loans for consumption.

  In terms of appraisal of the gratuitous income – which is indispensable for determining the amount to be added to and subtracted from the tax base – the tax administration prefers the methods specified by rules for property appraisal.

- From the provider's point of view, it was confirmed that gratuitous credits and loans, and loans for consumption shall not be eligible for the price test specified in Article 23(7) of the Income Tax Act.

  Unfortunately, the statement does not confirm the same position for the provider of gratuitous services.

- Should a company partner or cooperative member grant an interest-free credit or stand surety for their company or cooperative, the gratuitous income shall not be considered to increase the tax base of the company or cooperative.

  A similar approach (i.e. no gratuitous income on the part of the recipient-debtor) shall be applied by the tax administration in the case of standing surety for an obligation which involves a transfer of property with subsequent loan, or in the case of lease of machinery, equipment, forms and moulds intended for contractual production.

For information on specific cases which were discussed or for the detailed analysis of the influence of gratuitous income on your company's taxes, please feel free to contact our experts.

CHANGES TO IMMOVABLE PROPERTY ACQUISITION TAX

The Czech Chamber of Deputies is currently discussing a draft of regulation no. 340/2013 Coll. on immovable property acquisition tax which was submitted by the Senate. The regulation should introduce several important changes. Most notably, it should specify the purchaser as the tax payer in most cases of immovable property acquisition. At present the tax can be paid either by the purchaser or seller.

Another important change concerns the limitation of tax exemption on new flats and family houses only to finished buildings. The purchase of unfinished flat or family house will no longer be eligible for the tax exemption. In addition, guide values can be used to determine the values of plots without the "right to build", plots with weed trees (unwanted tree vegetation), hedges, fences or paved surfaces up to 25 sq. m. As a result, it will no longer be necessary to obtain an expert evaluation in these cases.

During the discussion in the parliament, MPs submitted several proposals for modifications. One of them concerns an exemption for municipalities, regions, and voluntary associations of municipalities – such subjects should not be obliged to pay the property acquisition tax.

Other proposals suggest lowering the immovable property acquisition tax rate to 3% or 2% or 1% or its complete removal (with reference to the tax's low annual revenue of ca CZK 10 billion).

Should the bill be endorsed by the Chamber of Deputies "as is", and later confirmed by the Senate and signed by the President, we can expect the law to be published in the Collection of Law no sooner than in June 2016, and come into force as of September.

TRANSFER PRICING INSPECTION ACTION PLAN, TRANSFER PRICING DOCUMENTATION AND THE AMADEUS DATABASE

The Czech tax administration keeps pace with the international activities of the OECD and EU (sometimes surpassing them). One of such areas includes the inspection of transfer prices and the related recent Transfer Pricing Inspection Action Plan.

There is no doubt the tax administration will increase the intensity of their inspection activities in the field. It is therefore very important to pay proper attention to the preparation for checks and inspections.

The best method of proving conformity of prices with the arm's length principles is the Transfer Pricing Documentation, which can often persuade the tax inspector that no tax inspection is actually necessary.

In this respect, it is advisable to use the Amadeus database, a very valuable tool for creating effective Transfer Pricing Documentation. The database includes information for the comparison of the company's financial results with conditions considered usual in the given market. The Amadeus database is widely used by revenue offices for their tax inspections.

PROXY, a.s. has extensive experience with keeping Transfer Pricing Documentation, as well as a license for the Amadeus database. This allows us to provide complete top-quality services in the area.

VALUE ADDED TAX

Below please find a current overview of VAT rates based on information received from our co-members in the European VAT Club.

For more information see www.vatclub.eu.

The information is valid as at 1 April 2016.

Member States	Code	Super Reduced Rate	Reduced Rate	Standard Rate	Parking Rate	Rate with effect from
Austria *[1]	AT	-	10	20	13	1 January 2016
Belgium	BE	-	6 / 12	21	12	1 January 2000
Bulgaria	BG		9	20	-	1 April 2011
Croatia	HR	-	5 / 13	25	-	1 January 2014
Cyprus	CY	-	5 / 9	19	-	13 January 2014
Czech Republic	CZ	10	15	21	-	1 January 2015
Denmark	DK	-	-	25	-	1 January 1992
Estonia	EE	-	9	20	-	1 July 2009
Finland	FI	-	10 / 14	24	-	1 January 2013
France	FR	2,1	5,5 / 10	20	-	1 January 2014
Germany	DE	-	7	19	-	1 January 2007
Greece (Mainland)	EL	-	6 / 13	23	-	20 July 2015
Greece (Aegean Islands)	EL	-	4 / 9	16		20 July 2015
Hungary	HU	-	5 / 18	27	-	1 January 2012
Ireland *[7]	IE	4,8	9 / 13,5	23	13,5	1 January 2012
Italy *[8]	IT	4 / 5	10	22	-	1 January 2016
Latvia	LV	-	12	21	-	1 July 2012
Lithuania	LT	-	5 / 9	21	-	1 September 2009
Luxembourg	LU	3	8	17	14	1 January 2015
Malta *[6]	MT	-	5 / 7	18	-	1 January 2011
Netherlands	NL	-	6	21	-	1 October 2012
Norway *[2]	NO	10	15	25		1 January 2016
Poland	PL		5 / 8	23	-	1 January 2011
Portugal	PT	6	13	23	13	1 January 2011
Portugal Madeira	PT	5	12	22		1 April 2012
Portugal Azores	PT	4	9	18		1 July 2015
Romania	RO		5 / 9	20	-	1 January 2016
Slovakia	SK	-	10	20	-	1 January 2011
Slovenia	SI	-	9,5	22	-	1 July 2013
Spain	ES	4	10	21	-	1 September 2012
Sweden *[3]	SE	-	6 / 12	25	-	1 January 1996
Switzerland *[4]	CH		2.5 / 3.8	8		1 January 2012
United Kingdom*[5]	UK	-	5	20	-	4 January 2011

Notes

- *[1] Austria - 13% rate for special supplies and services
- *[2] Norway - has a special rate for unprocessed fish sold to or through a fish cooperative 11.11%
- *[3] Sweden - Since 1 January 2012 restaurant and catering services are taxed at the reduced rate of 12% instead of 25%

  However, alcoholic beverages are still taxed at the standard rate of 25%
- *[4] Switzerland - has a special rate for hotel accommodation of 3.8%
- *[5] United Kingdom - zero-rate (exemption with the right of refund) for certain goods and services, e.g. most food and children´s clothes
- *[6] Malta - zero-rate foodstuffs, pharmaceuticals
- *[7] Ireland - zero-rate books, medical products, children´s clothing
- *[8] Italy - 5% rate for services supplied by social cooperatives in the field of healthcare and social wellbeing

THE BIGGEST TAX STAR OF THE YEAR AWARD

Results of the **6th Year of the Tax Advisor & Tax Company of the Year awards** for the year 2015 has been announced during the ceremony that had place in the hotel International Prague on 11 February 2016. Tax professionals and concerned laymen voted via internet to choose the best specialists in the different tax categories as well as the most taxpayers-friendly department of tax administration. Total of 7000 voters were voting on the best of 100 nominated tax advisors and specialists and 200 tax administration departments.

HLB PROXY had two strings to its bow for 2015:

* Ditta Hlaváčková, Partner of HLB Proxy, in the individual income tax category
* Magdaléna Vyškovská, tax advisor of HLB Proxy and winner of the category of international taxation in 2010 and 2013.

We are pleased to announce to our business partners, colleagues and friends that **Ditta Hlaváčková has been chosen as the Biggest Tax Star in the Individual Income Tax category**.

PROXY, a.s. / PROXY – AUDIT, s.r.o.

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