

ISSUE NO. 2 / MAY 2020

TAX FRESH



PROXY
TAX & AUDIT SERVICES

www.proxy.cz

A member of HLB International, the global advisory and accounting network

Dear business partners,

Our May issue of Tax Fresh presents the latest news in Czech legislation in the context of COVID-19 pandemic.

Best regards



Ditta Hlaváčková
Tax partner



Miroslav Mrázek
Tax partner

The information contained and accessed in the Bulletin – Tax Fresh is solely for general guidance and is intended to provide users with general information of interest. Whilst we endeavour to keep the Bulletin information correct, the information provided could be misinterpreted in practice. Therefore, we make no representations or warranties of any kind and we are not responsible for any loss or damages incurred. To find solutions to particular problems we recommend you consult with an HLB Proxy professional in the respective area.

COVID-19 PANDEMIC AND TRANSFER PRICING ISSUES



It is already clear that the impact of the COVID-19 pandemic will be far-reaching. From the point of view of transfer pricing, it is now necessary to consider a number of steps. Below we try to mention and highlight the necessary steps that should be actively managed and monitored from the perspective of transfer pricing to ensure their future defence before the tax administrator.

The Czech Republic is characterized by very intense network of the associated persons, when a number of such associated persons exercise the controlled transactions with their associated persons in the regime with limited risks. According to the theory of transfer pricing, the entities concerned are a so-called routine entities, among which rank the custom manufacturer, contractual manufacturer, agent, commission agent, distributor with limited risks or contractual provider of services. The essence of these routine entities is the performance of activity in achieving low, however stable profitability.

The tax administrator expects such a rate of profitability by default.

At the time of the COVID-19 pandemic, when almost all of the global economy is brought to a halt, or at least significantly paralysed by restrictions and quarantines, where all the affected states are facing a significant economic downturn, it is clear that the policy of transfer pricing in the group, the associated analytical work, including the documentation of transfer prices, will be greatly affected by this situation.

Therefore, the question is whether the tax administrator will consistently require routine entities to achieve projected profitability, or accept a decline in profitability or even a loss.

In our view, even though these are the routine entities, the theory of transfer pricing cannot be argued that such entities are risk-free entities. In fact, these entities bear at least the macroeconomic risk associated with the performance of their activities. The COVID-19 pandemic is a clear example of a negative impact on market conditions, i.e. on market risk.

For this reason, we believe that there is room for the so-called routine entities to advocate a deviation from expected profitability due to this very impact of the pandemic.

The preparation of arguments and evidence to support such a situation will be crucial.

For this reason, the companies should already count on the following steps in 2020:

- Revise the current policy of transfer prices and adjust it in accordance with the undertaken steps and, where appropriate, revise the new functional risk profile, if the group conducts internal restructuring due to the pandemic.
- Document duly conducted steps and thus support the deviations in expected profitability - this point is crucial, because it requires current action in terms of due archiving of all taken precautions and related communication within the group, to subsequently prove, as well as quantify, the impact of COVID-19 to company's business.

- It is necessary to take into account that the existing transfer pricing Documentation will most likely require thorough revisions – both in the section describing the functionally-risk profile and in the section of benchmarks that are based on the historical data prior to the pandemic.
- The subject of the adjustments can also be profit margins for so-called services with low added value (often referred to as “management fee” services), which are often treated in accordance with the D10 Guidance issued by the General Financial Directorate, which enables the application of the COST+ method with a 3 % to 7 % surcharge.
- Reconsider the exceptional transfer pricing adjustments at the end of 2020 depending on the adjustments made in the Transfer Pricing Documentation.
- Analyze the existing contractual arrangements in the context of the current situation, including the consideration of complementation/activation of the force majeure.
- Conclude new contractual arrangements in connection with the crisis services delivered by the parent company (if provided).

From the point of view of transfer pricing, it is important to understand the consequences of this pandemic, to carefully consider the valuation of transfer pricing in the context of all relevant aspects and to approach this issue with caution.

As outlined above, adjustment options certainly exist. However, they will require due preparation, i.e. a due “homework”.

Therefore, if necessary, do not hesitate to contact us.

UPCOMING AMENDMENT TO THE TAX CODE



Following the unsuccessful approval of the original amendment to the Tax Code, the Ministry of Finance prepared (in the order of several days) another amendment to the Tax Code. The new amendment is more favorable to tax entities than the original version on several points. The government has already approved the amendment and sent it to the Chamber of Deputies for approval at the end of April.

Compared to the original Code, the currently drawn amendment to the Code enables tolerance limit for paying tax, as the day of payment of the tax is considered to be the day of crediting money to the account of the tax administrator. At present, the tax entity shall incur interest on late payments starting on the fifth working day after the tax due date. There is a new proposal that the default interest arises from the fourth day following the original due date of the tax. At the same time, the default interest according to the Tax Code will newly correspond to the default interest according to the Civil Code (the current conditions set that default interest in the amount of the Czech National Bank repo rate increased by 14 pp, would newly be calculated in the amount of the Czech National Bank repo rate increased by 8 pp).

Taxpayers will certainly appreciate the maintenance of the 30-day period for the refund of the excesses (the original proposal counted with the refund of excesses within 45 days), and allowing the return of the undisputed part of the excess already in the course of the control procedure.

It is also proposed that the deadline for the filing of the tax return relating to the tax assessed for the accounting period, making of at least 12 months, is shifted by 1 month, i.e. 4 months after the end of the tax period, if the tax return is filed electronically (in the case of the taxpayer having the obligation determined by law to have the financial statement audited or whose tax return is processed and filed by the tax adviser, the period of 6 months after the end of the tax period will be maintained). Under the proposed transitional provision, this rule would already apply to tax returns for fiscal years started in 2020 if the amendment to the tax code takes effect at the beginning of 2021.

Another change will be the extension of the use of the tax information data-box, not only for obtaining selected information on record or tax register, but also as a means through which it will be possible to file applications to the tax administrator using the data in the tax data-box and acquire information from the documents and tax register as well as other alerts and notifications facilitating orientation in the fulfillment of the tax obligations.

The effectiveness of the proposed amendment to the Tax Code is proposed for 1 January 2021.

PROPOSAL TO ABOLISH THE REAL ESTATE TRANSFER TAX



In support of the economy, the Ministry of Finance proposes to abolish the real estate transfer tax. If the law is passed, the changes will apply to all immovable property registered in the cadaster in December 2019 and subsequently in 2020.

The proposed measure also includes the abolition of the application of the deduction of interest on newly concluded mortgage loans as a non-taxable part of the income tax base. Refinancing mortgage loans should be treated so that it is not considered as a new loan.

The Act will also include a so-called opt-in solution for people acquiring a newly-built immovable property that is exempt from the real estate transfer tax. If the taxpayer, within 30 days of the effective date of the law (or within the time limit for the submission of tax return), reported to the financial authority their interest to declare the tax and possibly pay the tax (in the case of newly-built property remains, of course, the exemption, and thus for such property the taxpayer will not pay the tax), it would be possible to further apply the interest deductions on a mortgage loan.

At the end of April, the draft law had still not been submitted for approval by the Parliament of the Czech Republic.

VAT RATE AMENDMENT EFFECTIVE FROM 1 MAY 2020 AND SUSPENSION OF THE EET



As of 1 May 2020, the VAT amendment entered into force, which relates in particular to the change in rates for selected types of goods and services. Originally, this amendment was associated with the launch of the last wave of electronic record of sales (EET). However, as a result of the state of emergency, the final stage of the EET was effectively postponed

by three months after the end of the emergency (currently the state of emergency is declared by 17 May 2020). However, the change in VAT rates for certain transactions from 1 May 2020 even without the launch of the last electronic record of sales (EET) wave will be effective.

The following supply of goods or services will be newly included in the reduced VAT rate of 10 %:

- Treatment and distribution of water through water distribution networks (previously at 15 %)
- Wastewater disposal and treatment, including other services related to these activities (previously at 15 %)
- Ebooks and audiobooks (previously at 21 %)
- Lending of books (previously at 21 %)
- Coloring pages, maps (previously at 15 %)

A reduced 10 % VAT rate will also fall on some other selected services. These are mainly services with a high proportion of human labour, for which VAT reductions are enabled by harmonised European legislation. The services concerned are:

- Cleaning services of indoor spaces conducted in people's homes (previously at 15 %)
- Window cleaning services performed in homes (previously at 15 %)
- Home care for children, elderly, sick and people with disabilities (previously at 15 %)
- Repair of shoes and leather goods (previously at 21 %)
- Repair and adjustment of clothing and textile products (previously at 21 %)
- Repair of bicycles (previously at 21 %)
- Hairdressing and barber services (previously at 21 %)
- Catering services and serving drinks (previously at 15 %), including draught beer (previously at 21 %). The reduction of VAT on draught beer to 10 % only applies to its sales within the catering service.

However, what cannot be considered a catering service is the currently widely applied purchase of takeaway food. Such purchase of food is from the point of view of VAT considered the supply of goods, and it is necessary to apply the VAT rate of 15 %. Catering services are services, which are supplied alongside with other services that complement the consumption of food and drinks and thus increase the benefit of consumption. Additional services mean e.g. restaurant staff services, the provision of premises for consumption of food and drinks, washable dishes and cutlery, toilets or locker rooms, etc.

We would also draw your attention to the fact, that with effect from 27 March 2020, the obligation to register sales is suspended (till the end of the state of emergency) for entities to which the obligation to record the sales existed already before the state of emergency. However, entrepreneurs can continue to keep a record of sales during this period on voluntary basis.

STATEMENT BY OECD ON SOLUTIONS RELATED TO COVID-19



At the turn of March and April 2020, the OECD contended how to proceed with measures of particular states in relation to COVID-19 from the point of view of international taxation, e.g. movement of people. According to the Statement on the model tax convention, the permanent establishment, for example, should not be taken as permanent from the point of view of fixed place or dependent representative when the employees of the foreign entity work from home. This view of the OECD is based on the fact that the aspect of permanence/habituality is not met.

Similarly, the OECD approaches to the concept of place of effective management, when due to the restriction of movement, the key management decisions could be carried out from a different state than company headquarters.

Although the Czech Tax Administration has not issued any statement on this issue, it is necessary to bear in mind that the opinion of the OECD should be taken as a recommendation only and each specific case should be addressed individually.

EXTENSION OF THE “ANTIVIRUS“ PROGRAM



The government of the Czech Republic extended the Antivirus Employment Support Program until the end of May 2020. The Antivirus Program stands for a compensation system when the state reimburses part of the wages, including the compulsory deductions, paid by the employers for a period of time when an obstacle to work on the side of the employer occurred due to the closure or restriction of operations because of the epidemic of the coronavirus, whether by a direct decision of the government in the framework of the announced preventive measures, or due to the secondary phenomena related to the epidemic.

To 24 April 2020, 42,731 applications were submitted in the Czech Republic and we are pleased to be among the 17,000 successfully processed applications. The Ministry of Labor and Social Affairs (MOLSA) publishes a continuously amended “Manual for Employees”. Today, we are already working with Version No. 4, and in the near future Version No. 5 will be available. In case of your interest, we are ready to help you with the entire program.

TERMINATION OF E101 (A1) FORMS



Portable forms E101/A1 are used to determine social security legislation relevance.

According to the coordination regulations No 883/2004 and No 987/2009, which replaced

regulations No 1408/71 and No 574/72, a ten-year transitional period was established for forms issued under the “old coordination regulations”.

Please note that on 30 April 2020 the E101 portable forms today’s known as A1 portable forms ceased to be valid as the transitional period ended.

We recommend that everyone checks especially those forms that have been issued, where the termination period is not indicated, i.e. the period for which they have been issued. In case of expiration, contact the relevant Social Security Administration and apply for an issuance of an A1 according to the current regulations.

PROXY, a.s., Plzeňská 3217/16, 150 00 Praha 5, TEL: +420 296 332 411, EMAIL: office@proxy.cz, **PROXY, a.s. – pobočka**, nám. Přemysla Otakara II./36, 370 01 České Budějovice, TEL: +420 386 100 011, EMAIL: officecb@proxy.cz, **PROXY, a.s. – pobočka**, nám. Míru 154/I, 339 01 Klatovy, TEL: +420 724 973 512, EMAIL: officekt@proxy.cz, **www.proxy.cz**, IČ: 15270301, DIČ: CZ15270301, zapsáno u Městského soudu v Praze pod B 612

PROXY – AUDIT, s.r.o., Plzeňská 3217/16, 150 00 Praha 5, TEL: +420 296 332 411, EMAIL: office@proxy.cz, **PROXY – AUDIT, s.r.o. – pobočka**, nám. Přemysla Otakara II./36, 370 01 České Budějovice, TEL: +420 386 100 011, EMAIL: officecb@proxy.cz, **PROXY, a.s. – AUDIT, s.r.o. – pobočka**, nám. Míru 154/I, 339 01 Klatovy, TEL: +420 724 973 512, EMAIL: officekt@proxy.cz **www.proxy.cz**, IČ: 49684612, DIČ: CZ49684612, zapsáno u Městského soudu v Praze pod C 23375

TOGETHER WE MAKE IT HAPPEN

