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Information on Law, Taxes and Economics in the Czech Republic

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Content:

→ Law

New obligation relating to the recycling contribution

Do you trade in electrical equipment, batteries, accumulators, tires or vehicles? Do you manufacture or distribute them? You must now indicate the so-called recycling allowance separately on your tax-related documents.

Alena Tomsová
Rödl & Partner Prague

Effective 1 January 2021, Act No. 542/2020 Sb., on end-of-life products was adopted in 2020 in connection with the adoption of the new Waste Act. The Act incorporates the relevant European Union regulations, namely the European Parliament and Council Directives on waste, on waste electrical and electronic equipment, on batteries and accumulators, including waste batteries and accumulators (also in relation to marketing) and on end-of-life vehicles, as well as the directly applicable Commission Regulations (EU) on the recycling of waste batteries and accumulators and on the registration and reporting of producers of electrical and electronic equipment. The compatible European regulation gives EU Member States the power to require manufacturers to inform buyers when selling new products about the costs of their environmentally friendly collection, treatment and disposal. The Czech legislator apparently took advantage of the authorisation and reflected it in Section 73 of the new Act.

The scope of the law

The Act applies to selected products, regardless of whether they are placed on the market on their own or as parts of or accessories to other products, from their manufacture and placing on the market to the treatment of the waste resulting from them. Selected products include electrical equipment, batteries and accumulators, tires and vehicles.

Obligation to indicate the recycling contribution

The law imposes an obligation on the producer of electrical equipment, the distributor and the so-called last seller to "indicate separately from the price (...) the costs of the take-back, treatment, recovery and disposal of waste electrical equipment per one piece of new electrical equipment or one kilogram of new electrical equipment, in particular by means of a separate entry on the tax document in accordance with the Value Added Tax Act" when selling new electrical equipment. Those costs may not exceed the costs known to the producer of the electrical equipment at the time the new electrical equipment is placed on the market or an estimate of the estimated costs if the costs are incurred by the producer of the electrical equipment after market placement. The separate disclosure of costs will not affect obligations regulated by pricing legislation (Act No 526/1990 Sb., on prices).

A manufacturer is defined as "a manufacturer of electrical equipment, a manufacturer of batteries or accumulators, a manufacturer of tires or a manufacturer of vehicles". A distributor is defined as "a person who, as part of his business, places a selected product on the market in the supply chain". A retailer is then defined as "a person who, irrespective of the method of sale, including the use of means of distance communication, supplies, in the course of its business, to the end user in the Czech Republic, selected products, vehicles, electrical equipment, tires or other products incorporating or accompanied by batteries or accumulators, or vehicles or other functional units incorporating or accompanied by tires".

Sanctions

The law treats cases where the manufacturer, distributor or retailer does not separately state the costs or states them in contradiction with the law as "other offences" committed by legal entities and natural persons. For these offences, the Czech Trade Inspection Authority may impose a fine of up to CZK 500,000 on the manufacturer, distributor or retailer.

The impact of the Act on the business of commercial companies

Until the end of 2020, it was up to the manufacturers, distributors or retailers to decide whether to indicate the recycling contribution on tax documents. Now, as mentioned above, this obligation is imposed directly by law on all these entities.

Thus, the law effectively impacts the business of many commercial companies and affects their invoicing. Therefore, it is very useful to identify the areas of economic activity of these companies and to assess whether or not the legal obligation to indicate the recycling contribution as a separate item on the tax invoice under the VAT Act applies to a particular company within the meaning of the Act. The amount of the possible sanction (fine) could significantly affect the economy of the companies in the event of their non-compliance (i.e. not complying) with the legal obligation, especially in view of the fact that the wording of the law does not preclude the imposition of a fine repeatedly. Therefore, in order to avoid the negative impact of the law on your business, we are ready to provide you with comprehensive services, both in the legal and tax field.

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→ Taxes

EU list of non-cooperative tax jurisdictions updated

On 22 February 2021, the Council of the European Union issued a press release announcing the re-updating of the existing list of so-called non-cooperative tax jurisdictions. These are countries that have not yet taken appropriate steps in relation to planned tax reforms and have thus been unable to meet their obligations in the area of international tax cooperation.

This list, which was first established by the Council of the European Union in December 2017 and which we have previously reported on in our previous Newsletters, currently includes the following countries following a review by the European Union: American Samoa, Anguilla, Dominica, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, US Virgin Islands, Vanuatu and Seychelles.

The European Union has long sought to improve tax governance internationally. The EU's list of non-cooperative tax jurisdictions is a key tool in the fight against money laundering, tax evasion and any unlawful conduct consisting of tax evasion or avoidance.

The implementation of transactions with persons based in a non-cooperative state may have a number of tax implications for Czech entities, including in particular the obligation to apply the highest withholding tax rate (35%) to such income that is subject to it under Czech legislation.

The Council of the European Union regularly reviews the fulfilment of the established criteria and obligations resulting from the adoption of reforms under international tax standards and in this context carries out an appropriate revision and subsequent update of the list of non-cooperating states. The current list, which contains only third countries supporting so-called 'unfair tax practices', has been updated twice a year since 2020. The next review is to be carried out again in October this year.

It may be assumed that this trend of regular scrutiny by representatives of the Council of the European Union will continue unchanged in the coming years.

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→ Taxes

Brexit from an income tax perspective

The departure of the United Kingdom of Great Britain and Northern Ireland from the European Union on 31 December 2020 ("Brexit") brings with it not only a number of economic changes, new rules and restrictions, it also has an impact on taxation.

Robert Němeček
Rödl & Partner Prague

We recently reported on the impact Brexit has from the perspective of value added tax (related information has been issued by the Czech General Financial Directorate) and also from the perspective of social insurance. Below we briefly outline the impact Brexit has on income taxation.

So what are the main changes from 1 January 2021 from the perspective of business corporations and what should you look out for?

Until now, interest and royalty payments paid from the Czech Republic to the UK have been exempt from withholding tax under Czech legislation, which has implemented the relevant EU Directive. After 31 December 2020, it will be necessary to examine whether the conditions for the application of the double taxation treaty between the Czech Republic and the United Kingdom are met in respect of such payments and, depending on the type of income and the treaty, to apply withholding tax where appropriate.

As a result of Brexit, Czech entities paying profit shares to the UK will not be able to benefit from the automatic exemption which, like the exemption for royalties and interest, was based on an EU directive and which has been implemented in the past in Czech legislation. In the case of such payments, again, the provisions of the Double Taxation Treaty between the Czech Republic and the UK should be the primary rule. Conversely, profit shares received from the UK by Czech tax residents may be exempt from taxation in the Czech Republic under certain conditions.

Attention should also be paid to situations where payments are made to the UK which are not subject to Czech withholding tax in the Czech Republic. In selected cases, an obligation to withhold collateral tax may arise on such payments, and this obligation is borne by the Czech entity making the payment.

In addition to the above-mentioned effects, new restrictions in the case of cross-border conversions must be taken into account, where it will no longer be possible to benefit from the advantages previously allowed by the European Directives.

For the sake of completeness, we would like to point out that Brexit will also impact the taxation of personal income, where UK citizens will no longer benefit from the advantages that EU citizens can enjoy.

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→ Taxes

Decision on remission of sanctions for February 2021

The Minister of Finance issued a decision on the remission of value added tax accessories due to an emergency (hereinafter referred to as the “Decision”) in connection with the emergency measures on the restriction of free movement in the period from 1 March to 21 March 2021 announced by the Government of the Czech Republic following the outbreak and spread of the SARS-CoV-2 virus.

Under the Decision, VAT payers (and identified persons) do not have to pay any penalties or interest for filing their VAT return or paying their VAT obligations for February 2021 late. The remission is automatic under the condition that the taxpayer fulfils its obligations by 15 April 2021 at the latest. Remission also applies to the penalty for late filing relating to the additional VAT return due by the end of March 2021, if it is filed by 15 April 2021.

The Finance Minister will also remit certain penalties arising from obligations relating to the February 2021 VAT control statement or where the deadline for compliance with those obligations runs in part between 1 March and 21 March 2021 and the obligation is complied with again by 15 April 2021.

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→ Taxes

Utilisation of VAT in compensation for unused material

According to the opinion of the General Financial Directorate, compensation for unused material, material that is either sold to third parties or disposed of on the basis of the customer’s instructions, can represent, from a VAT point of view, compensation for a rendered service.

Michael Pleva, Adéla Gabrielová
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The Coordinating Committee of the Chamber of Tax Advisors discussed situations involving premature discontinuation of the production process and the potential VAT impacts. It is quite usual to encounter situations where a seller is arranging the production of pre-specified products for the seller’s customer. As a result of changes in demand for the products involved, however, the customer may decide to suspend the production process or to discontinue the production process altogether.

Based on such a decision, the seller usually ends up with unused material in the warehouse and such unused material may be sold to other parties in accordance with contractual covenants or may be physically disposed of. This causes a loss to arise for the seller, a loss that the customer provides compensation for. And since the relevant supplies are disposed of, on the basis of the customer’s decision, in the Czech Republic, we are left with the question of what VAT procedure should be used for such compensation.

Is the supply subject to VAT?

First we need to determine whether the compensation for unused material is subject to value added tax. If the compensation were to be viewed as compensation for damage or a contractual penalty ensuing from a breach of the conditions stipulated in an agreement, the transaction would probably not be subject to VAT.

In the opinion of the submitters of the opinion, the decisive factor is how the transaction was set up contractually. And since the possibility to discontinue the production process is provided for in the relevant agreement, the situation cannot represent compensation for damage or a contractual penalty for a breach of contractual conditions.

Supply of goods or provision of a service?

It is additionally necessary to make a distinction between the provision of a service and the supply of goods for consideration, which becomes even more important in the case of cross-border transactions. Since the supply of goods takes place without transportation, VAT should be remitted on the amount received, typically at a rate of 21%. By contrast, in the case of a service provided to a foreign entity that does not have an establishment in the Czech Republic, the reverse charge mechanism will be applied, meaning that VAT will not be applied to the transaction in the Czech Republic.

Opinion of the General Financial Directorate

It first needs to be stated that the General Financial Directorate views the contribution as a very general contribution without a clear conclusion. Fortunately, however, the General Financial Directorate brings positive conclusions for all taxable entities that need to deal with such cases.

In a given situation, the decisive factor is always the economic and business reality of the transaction concerned, and the contractual covenants between the parties. This means that each situation must be assessed on an individual basis. If the agreement clearly stipulates the conditions for a settlement of costs arising due to unused material, a disposal of the unused inventory will be deemed to constitute a service. It also applies that the service concerned cannot be assigned to the "main" supply (i.e. to the original supply of goods) but must be viewed as a separate transaction.

In view of the foregoing, we recommend duly reviewing the wording of your agreements, and, if necessary, clearly stipulating the rights and obligations of all entities involved. This will significantly reduce the tax risk on your side.

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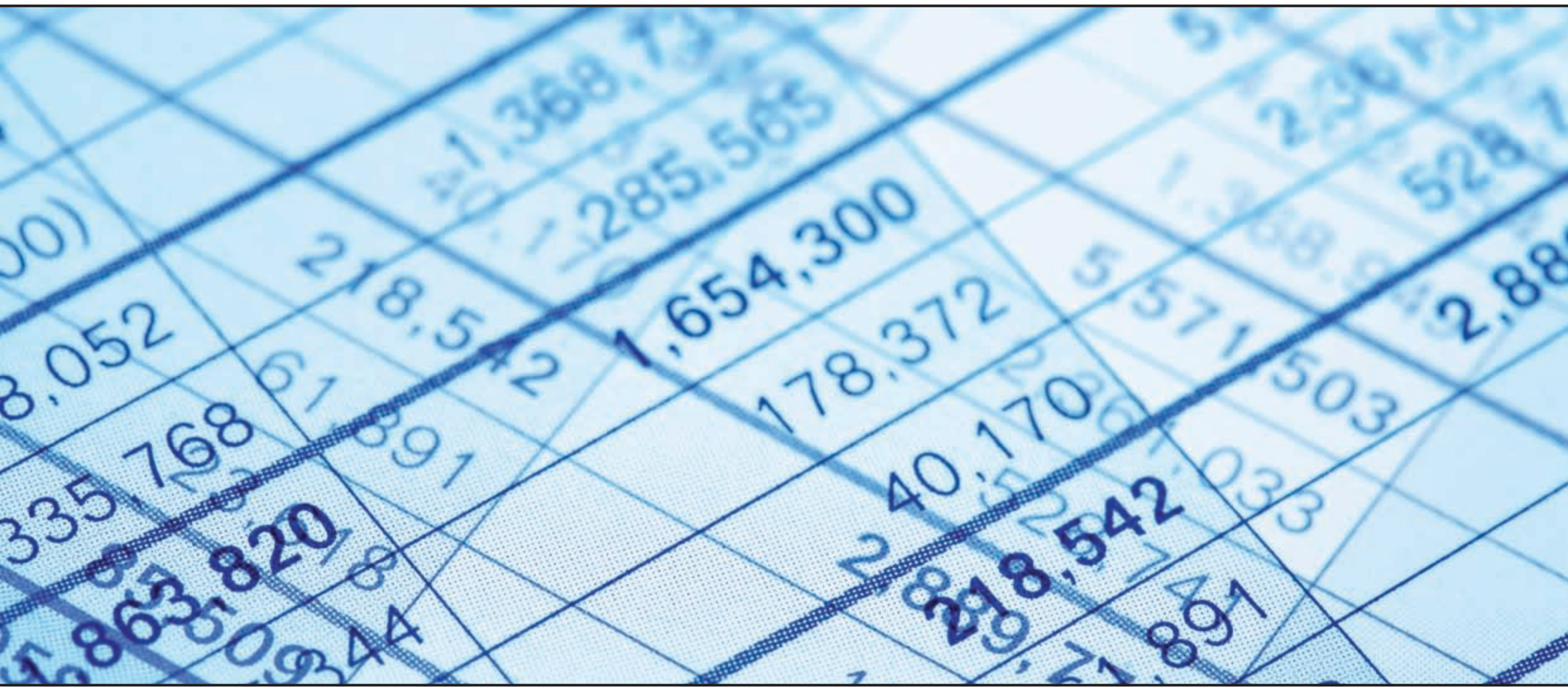

→ Taxes

The right to deduct VAT on insurance related to the export of goods

The Coordination Committee of the General Financial Directorate and the Chamber of Tax Advisors (KOOV) discussed in detail the possibility of claiming VAT deduction for insurance services provided in connection with the export of goods.

The provision of insurance is one of the services that are generally exempt from VAT without the right to deduct. However, in the case of insurance and certain financial services related to the export of goods, VAT can be deducted on the related inputs.

The KOOV concluded that the VAT on the supplies received in connection with the insurance provided is deductible if the insurance is provided directly to a Czech manufacturer who is also an exporter of goods to a third country. On the contrary, if the insurance is an insurance where the insured and the insurer is a person different from the exporter, e.g. a bank, the insurance company is not entitled to deduct VAT on the benefits received in connection with this insurance due to the lack of a direct link with the export.

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→ Taxes

General Financial Directorate on ATAD – limitation of excessive borrowing costs

In the second half of January this year, the General Financial Directorate (GFD) issued a document titled Information on Measures Resulting from the Implementation of the So-called Anti-Tax Avoidance Directive (“Information”), which was stitched together in 2017 as a result of the initiative taken up by the Organisation for Economic Co-operation and Development in an effort to combat the ever-growing tendency of selected taxpayers trying to avoid their tax obligations. The Anti-Tax Avoidance Directive (“ATAD”) was transposed into Czech legislation by an amendment to the Income Tax Act and as such, with effect from 1 April 2019, it established several completely new, but quite fundamental, rules for corporate taxpayers and their permanent establishments.

Robert Němeček, Filip Straka
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The long-awaited Information issued by the GFD contains answers to a number of practical questions that have arisen in connection with the implementation of the ATAD. Below we provide a summary of some of the main conclusions and explanations relating to individual areas (i.e. limitation of deductibility of excessive borrowing costs, exit tax, rules for taxation of controlled foreign companies and hybrid mismatches).

Limitations on the deductibility of excessive borrowing costs

The rule limiting the deductibility of so-called excessive borrowing costs was adopted to prevent an increase in the number of corporate taxpayers using debt financing to excessively reduce the tax base and potentially shift profits to lower tax countries.

In addition to the general classification of excessive borrowing costs and the period for which the tax deductibility limit of CZK 80,000,000 for excessive borrowing costs can be applied, the Information addresses issues related to the specification of selected borrowing costs as defined by the law.

The GFD also states, in relation to very frequent questions related to the inclusion of exchange rate differences in borrowing costs, that only those exchange rate differences that are directly related to the liability arising from borrowing costs are included in borrowing costs. In this context, the Information specifies the derivatives that are treated as borrowing costs for these purposes. The GFD then goes on to clarify on what basis the interest included in consideration will be classified as a borrowing cost or under what circumstances so-called capitalised interest may qualify as a borrowing cost.

Notwithstanding legislation allowing, under certain conditions, the economic result in a given taxable period to be reduced by the amount by which the economic result was increased in a previous taxable period as a result of the limitation on the deductibility of excessive borrowing costs, the GFD also points out that this possibility does not automatically pass to the legal successor of the entity in the event of a transformation.

Last but not least, in its Information the GFD addresses the issue of uniform and correct reporting of the relevant adjustment to the economic result in the corporate income tax return form, and in this context notes that for this purpose new lines have been added to the tax return form with a link to the relevant annexes and related tables.

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→ Taxes

Selected waivers responding to Covid-19

The Ministry of Finance waivers penalties for the late filing of income tax statements for the 2020 tax year as it does any late payment interest associated with the late payment of tax, provided:

- The taxpayer files his tax return and pays the related tax liability no later than by 3 May 2021 (statutory obligation due 1 April 2021),
- The taxpayer files his tax return and pays the related tax liability by 1 June 2021 at the latest (statutory obligation due 3 May 2021, i.e. extended deadline due to electronic filing).

The same deadlines apply to personal income taxpayers who have incurred a penalty for failing to report exempt income for the 2020 tax year.

The Government has put in place a two-month extension of the VAT waiver for the supply of at least FFP2 protection class filter masks and respirators, i.e. until 3 June 2021. If the supplier of respirators discloses VAT on the tax invoice, it must declare this VAT despite the waiver. The buyer cannot claim a VAT deduction on such a receipt, but there is a debate in the expert community as to whether this ban is even legal.

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→ Taxes

Does a suspension of extraordinary depreciation of assets have an impact on the tax deductibility of the extraordinary depreciation?

If a taxable entity suspends the extraordinary depreciation of an asset, a subsequent extraordinary depreciation of such asset claimed by the taxable entity cannot be viewed as expenses expended for achieving, ensuring and maintaining taxable income

Jakub Šotník
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IThe Supreme Administrative Court addressed the issue of extraordinary depreciation, a possibility that had been incorporated into the Act on Income Tax more than ten years ago in response to the global financial crisis. At that time, such extraordinary depreciation pertained to selected categories of assets purchased during the period from 1 January 2009 to 30 June 2010 and enabled taxable entities to claim accelerated depreciation on such assets. At first glance it could seem that the Supreme Administrative Court was addressing a possibility that is no longer topical at the present time, but in fact this is not the case. This is because extraordinary depreciation was "revived" when lawmakers amended the legislative treatment of extraordinary depreciation with effect as at 1 January 2021. In fact, lawmakers amended the legislative treatment of extraordinary depreciation only to the extent of amending the time period during which such assets must have been purchased in order to meet the eligibility requirements for such extraordinary depreciation. So the Supreme Administrative Court's judgment comes at a most opportune time, since many taxable entities are presently thinking about using such extraordinary depreciation, since lawmakers have again made it possible to do so.

The disputed issue addressed by the aforementioned judgment was the issue of whether it is possible for a taxable entity that is claiming extraordinary depreciation to suspend the claiming of such extraordinary depreciation. In the case under review, the taxable entity had purchased a fixed asset in 2009, specifically an automobile, and had also claimed in that year, pursuant to the provisions of Section 30a of the Act on Income Tax, extraordinary depreciation on the purchase cost of the automobile. In the 2010 tax year, the taxable entity decided not to claim depreciation on the asset. In the 2011 tax year, however, the taxable entity again claimed such extraordinary depreciation and additionally also included a part of the extraordinary depreciation that the taxable entity did not claim in 2010.

> A taxable entity that is claiming extraordinary depreciation is not entitled to suspend the claiming of such depreciation

During a subsequent tax audit in respect of the 2011 tax year, the tax authority concluded that the taxable entity was not eligible to claim the extraordinary depreciation in such tax year. Such conclusion on the part of the tax authority was based on the fact that the taxable entity did not claim the extraordinary depreciation in the 2010 tax year. The tax authority took the view that by failing to claim the extraordinary depreciation in the 2010 tax year, the taxable entity suspended the process of claiming depreciation and thereby breached the statutory requirement for eligibility for claiming such extraordinary depreciation. In connection with this, the tax authority emphasised that claiming such extraordinary depreciation without any suspensions is a requirement for eligibility for such extraordinary depreciation. As the tax authority additionally noted, there was nothing preventing the taxable entity from claiming the extraordinary depreciation in the 2010 tax year. These conclusions were subsequently affirmed by the regional court.

The taxable entity filed a cassation complaint in which it argued that it did not cause the period for claiming the extraordinary depreciation to be extended by the fact that it had not claimed the extraordinary depreciation in 2010. The taxable entity further argued that it had claimed the extraordinary depreciation only in the amount that it had been entitled to claim. The taxable entity also made reference to Section 26 (8) of the Act on Income Tax, which allows taxable entities to decide not to claim depreciation, and argued that this did not mean that the claiming of depreciation had been suspended. In the taxable entity's view, the procedure followed by the taxable entity could not therefore be classified as a suspension of depreciation.

The Supreme Administrative Court rejected the argumentation put forward by the taxable entity and stated that according to the statutory definition, tax-deductible depreciation consisted of the depreciation of tangible assets recorded on a taxable entity's books, specifically the depreciation of tangible assets that are used for ensuring taxable income, where such assets are depreciated into the expenses (costs) incurred in order to ensure such income. From this the court concluded that if the taxable entity had commenced depreciation of the asset concerned in the 2009 tax year and had failed to claim such depreciation in the 2010 tax year, then this means that within the meaning of the Act on Income Tax the taxable entity did not claim depreciation in that year, and this can only lead to one conclusion, the conclusion that the taxable entity had suspended depreciation in 2010.

The Supreme Administrative Court emphasised that there is no doubt that the ability to claim tax depreciation is a right, but not an obligation, of taxable entities. However, if a taxable entity elects to exercise such right, it is obligated to proceed in the manner stipulated by law, and the law did clearly specify the procedure to be used for extraordinary depreciation. In the reviewed case, however, the taxable entity had failed to comply with such procedure and therefore the extraordinary depreciation claimed in respect of the 2011 tax year cannot be treated as a tax deductible expense.

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