Rödl & Partner

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Content:

→ Law

Is easier enforcement of cross-border claims on the horizon?

At the beginning of July 2019, the Hague Conference on Private International Law adopted the Convention on the Recognition and Enforcement of Foreign Judgments in Civil or Commercial Matters (the Convention). In the future, the Convention may be an important tool for international commercial practice, particularly in relation to cross-border recovery of debts and other claims. This article examines the current state of recognition and enforcement of foreign judgments and possible future developments in relation to the Convention.

Alice Kubová Bártková, Adam Kotyza
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If the obligated party (the debtor) does not have sufficient assets in the territory of the state where the relevant judgment was issued, the entitled party (the creditor) has no choice but to seek recognition and enforcement of the judgment in another state. Recognition of a judgment means that the foreign judgment is given the same legal effect as a domestic judgment. Enforcement then consists of compelling the debtor to fulfil the obligation imposed on him by the decision (for example, to pay the amount due).

Convention on the Recognition and Enforcement of Foreign Judgments awaits ratification.

Recognition and enforcement of foreign judgments is governed by a number of supranational laws, including EU regulations and international conventions. However, their shortcoming is their limited territorial scope. EU regulations apply only in the territory of EU Member States and international conventions only in the territory of states that have acceded to the convention concerned. However, so far, there is still no international convention to which most of the world's states would be parties and which would regulate the recognition and enforcement of foreign judgments.

If an EU Regulation or an international convention does not have territorial jurisdiction both in the state where the judgment was issued and in the state where the entitled party (the creditor) seeks recognition and enforcement of the judgment, the entitled party is in a difficult situation. The entitled party has to seek recognition and enforcement of the judgment under the national law of the state concerned.

The national laws of each country governing the recognition and enforcement of so-called third-country judgments may contain very different rules. Such rules may be so strict that the entitled party will ultimately have no choice but to initiate new legal proceedings in that state.

For Czech entities, it may be problematic if they have agreed in a contract with a business partner from a third country outside the EU that the Czech courts have jurisdiction, but the business partner has no assets or insufficient assets in the Czech Republic. In this situation, although they can in principle obtain the issuance of a judgment by the Czech courts, the recognition and enforcement of the judgment will usually have to be dealt with in the territory of the third state in which the business partner has its headquarters (registered office) since that would usually also be the state where the business partner has sufficient assets. The recognition and enforcement of a judgment from the Czech Republic will be governed exclusively by the laws of that third state.

It is precisely this dismal state of affairs that the Convention aims to address. Its ambition is to achieve in the field of recognition and enforcement of foreign judgments a similar breakthrough to that achieved by the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention). That convention currently has 156 signatory states and its worldwide significance for international commercial relations is thus absolutely fundamental.

The 2019 Convention undoubtedly has the prerequisites for achieving this. Indeed, legal experts from a number of countries, including the EU, the US and China, have been involved in the drafting of the Convention for many years. This has therefore ensured the adoption of a high-quality, widely acceptable text. The key for the future, however, will be whether enough states will accede to the Convention so that it can take on global significance.

Since the adoption of the Convention on 2 July 2019, only six states have signed it so far (Costa Rica, Uruguay, Ukraine, Israel, Russia and the USA). However, none of these states has ratified the Convention as yet, and decades may pass between signing and ratification, or a state that has signed it may not ultimately ratify it at all. Ratification by at least two states is one of the conditions for the Convention to enter into force.

The EU may also have an important role to play in the future of the Convention, as it has exclusive competence to accede to the Convention following the 2006 CJEU opinion. A proposal for accession to the Convention was submitted by the European Commission to the European Parliament on 16 July 2021.

So, one can only hope that the EU and other countries will accede to the Convention as soon as possible and that it will fulfil its promised global potential.

In light of the foregoing, the most feasible solution to the problem of enforcement of decisions in relations with business partners from third countries continues to be the practice of negotiating a proper arbitration clause in accordance with the New York Convention. Our advisors will be pleased to assist you with the preparation of a suitable arbitration clause, as well as with the potential subsequent enforcement of a foreign arbitral award or foreign court decision in the Czech Republic.

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→ Taxes

VAT on early termination of energy supplies

The Coordination Committee of the Chamber of Tax Advisors and the General Financial Directorate met to unify the interpretation of how VAT is applied when the parties' compensation is subject to tax in the event of early termination of an energy supply contract or the non-delivery of the agreed amount of energy. The General Financial Directorate confirmed that this is a supply of a service subject to the standard VAT rate.

Klára Sauerová, Lucie Kukrálová
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The aim was to clarify and unify the interpretation of the application of VAT in the event that the provider of heat, electricity, gas, and the like agrees with the customer to terminate the contract early or if the customer for whatever any reason fails to collect a certain amount of energy. The following three situations were discussed.

Situation One and Situation Two concerned the simple early termination of the contractual relationship by the parties' mutual agreement, where the agreed amount of energy was not supplied at the pre-agreed price. When it comes to the early termination of a contract, one of the parties

must compensate the other party for the unsupplied or uncollected energy, which was calculated as the product of the amount of unsupplied energy and the difference between the pre-agreed price and the market price at the date of termination. If the market price at the date of termination of the contractual relationship was higher than the pre-agreed price, the provider compensates the customer; if the market price at the date of termination of the contractual relationship was lower, the customer compensates the provider.

Accordingly, compensation does not constitute a supply of goods within the meaning of s. 2 of the Value Added Tax Act, since there was no supply of energy. Compensation concerns only unsupplied or uncollected energy. According to the submitter's conclusion, it is therefore a service supplied with a place of supply in the domestic territory subject to the standard VAT rate. The General Financial Directorate confirmed the conclusion.

Situation Three concerned the so-called compression of multiple contracts. Compression means entering into several contractual relationships for the sale and purchase of energy. When these contractual relationships are terminated early, the parties may revert to compression and then their claims and liabilities are set off against each other to the extent that they overlap. Neither party therefore provides any consideration. Any difference remaining after the set-off of claims and liabilities constitutes compensation for energy not supplied. According to the submitter, this difference is treated as a separate financial claim or liability, which is not considered a taxable supply, as it is a financial supply not subject to VAT. The General Financial Directorate disagreed with this conclusion and considered that this third situation should be treated in the same way as the first two, as it is a compensation for unsupplied energy where the provider and the customer agree that one of them is entitled to compensation. The GFD therefore concluded that the compensation should again constitute a supply of a service with a place of supply in the domestic territory subject to the standard VAT rate.

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→ Taxes

Promoting low-emission mobility

The Czech Government adopted a law the aim of which is to promote low-emission mobility; it came into effect on 1 July 2022. It adds value to low-emission vehicles when they are also used by employees for private purposes and reduces the tax depreciation period for charging stations (wallboxes).

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Low-emission vehicle for business and private use

Where low-emission vehicles are concerned, the Act reduces the amount of the employee's non-cash income from the use of the company vehicle for private purposes from the current 1% to 0.5% of the entry price of the vehicle.

A low-emission vehicle is a category M1, M2 or N1 road vehicle which does not exceed the CO_2 emission limit of 50 g/km and 80% of the emission limits for air pollutants in real operation as laid down in Annex I to Regulation (EC) No 715/2007 of the European Parliament and of the Council of 20 June 2007 on type-approval of motor vehicles with respect to emissions from light passenger cars and light commercial vehicles (Euro 5 and Euro 6), as amended.

Non-monetary income in a multi-vehicle per month situation is calculated as follows.

If several motor vehicles, some of which are low-emission, are provided free of charge to

an employee successively in one month, the value weighted towards the type of vehicle with the highest price will be used for the calculation. If the most expensive vehicle is a low-emission vehicle, a value of 0.5% of the entry price of that low-emission vehicle will be used; if the most expensive vehicle is a non-low-emission vehicle, a value of 1% of the entry price of that vehicle will be used.

Similarly, in a situation where an employee will have successively more than one non-low-emission vehicle and more than one low-emission vehicle in a calendar month, the procedure is the same, the employee's income will be the income of the entry price of the vehicle with the highest entry price. This procedure also applies in the case of a successive rotation of the two categories of vehicles.

In the case where several vehicles, both low-emission and non-low-emission, are provided free of charge to the employee in the same month, the income will be calculated in two steps. In the first step, the income from low-emission vehicles and the income from non-low-emission vehicles will be calculated separately. In both cases, the sum of the vehicle prices is multiplied by the value appropriate to the category – 0.5 or 1%. These two amounts are then added together to determine the non-cash employment income for the month.

The amendment will take effect from 1 July 2022.

The amended procedure for determining non-cash income will apply for the 2022 tax year. The procedure in force before the date of entry into force of this Act (i.e. 1%) will be applied when calculating wages and calculating the advance personal income tax on employment income for the calendar months of 2022 ending before the date of entry into force of this Act (i.e. for wages for January to June 2022).

For the months of January to June 2022, the amendment, i.e. the application of the 0.5% income rate for low-emission vehicles, will only be taken into account in the annual settlement of advances and tax credit for 2022 or in the tax return. However, this does not apply to social security and health insurance, for which the assessment base for January to June 2022 will not be additionally reduced.

Reduction of the tax depreciation period for charging stations (wallboxes)

The amendment reduces the tax depreciation period for charging stations (wallboxes) from 10 years to 5 years by reclassifying charging stations (wallboxes) from depreciation group 3 to depreciation group 2. The change applies to charging stations acquired after 1 July 2022. Where previously acquired stations are concerned, reclassification from depreciation group 3 to depreciation group 2 is optional.

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→ Taxes

Proposal to introduce a discount on social security contributions

In an attempt to mitigate rising prices and the energy crisis, the Czech Government has come up with some sort of a family package. It includes a discount on social security contributions that could encourage more flexible work arrangements. Flexible-work arrangements are defined as working between 8 and 30 hours per week or less than 138 hours per month. Any excess over the average hourly rate will also be considered, in which case the discount will not be available.

The discount is 5% of the aggregate of the assessment bases of selected employees. The discount is available to employees who fall into the following groups:

- Persons over 55 years of age;
- Persons caring for a child under 10 years of age;
- Persons caring for a relative under 10 years of age who is dependent on the assistance of another person;
- Persons studying at secondary school or university;
- Persons undergoing retraining;
- Persons with disabilities;
- Persons under 21 years of age.

Anyone who intends to claim the discount must notify the authorities in advance. The discount is applicable for the given month and a separate record of one meeting the conditions for claiming the discount is required.

The Government plans for the idea to take effect six months after the law has been passed.

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→ Taxes

VAT regime for early termination of finance leaseback

Recently, the Coordination Committee of the Chamber of Tax Advisors and the General Financial Directorate discussed VAT issues in connection with finance leaseback. They came to the conclusion that, in certain circumstances, these types of leases do not involve the supply of goods, as the whole transaction constitutes a service in the form of financing. However, the VAT implications in a situation where the lessee ceases to fulfil its obligations to the leasing company in a proper and timely manner remained unresolved. The situation has therefore been discussed by a separate coordination committee. So what about the early termination of a finance leaseback?

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In essence, the leased item represents a form of security instrument for the leasing company, which is its legal owner, giving it the opportunity to "cash in" on it in the event that the lessee ceases to properly and timely perform its obligations under the lease agreement. In such a situation, the leased item will be taken by the leasing company, which will presumably try to monetise it and pay its claim on the lessee from the proceeds of the sale.

The removal of the leased item by the leasing company due to non-payment by the lessee is considered a supply of goods subject to the reverse charge.

In the past, the Coordination Committee already confirmed that the removal of an item used as a security instrument constitutes a sale of goods for VAT purposes, i.e. the lessee will sell the item to the leasing company. At the same time, the General Financial Directorate has confirmed in its previous information that the reverse charge regime applies in particular to the transfer of security.

Therefore, based on the above-mentioned arguments, the Coordination Committee and the General Financial Directorate agreed that the reverse charge regime would also apply to finance lease transactions, as this is an analogous situation. And so, the obligation to pay VAT on the sale of the item of a lease terminated early due to the lessee not paying the leasing company will be borne by the leasing company.

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→ Taxes

Financial Administration simplifies registration for foreign individuals to DIS+

The original Tax Information Boxes were switched off at the beginning of this year and only the Tax Information Boxes Plus (DIS+) have remained in operation since then.

In practice, however, DIS+ was only available to Czech citizens, as in order to set up a DIS+, it was necessary to first pair the person with the data listed in the population register of the Czech Republic. This is where foreign persons ran into problems, as when setting up their DIS+, it was not possible to successfully pair them with the aforementioned population register.

Things have changed and the Financial Administration will now allow foreign persons who have a data box or a guaranteed identity (NIA) to set up a DIS+ using a special electronic form. This is good news for all foreign persons who want to have their Czech tax obligations under control and also for Czech companies whose managing director (governing body) is a foreign person.

We have extensive experience with setting up DIS+. If you are interested, please do not hesitate to contact us. Our experts can help you set up a DIS+ and even a data box abroad. And if you want to have a truly comprehensive overview of all your Czech tax obligations, we will also be happy to arrange regular monitoring of your DIS+.

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→ Taxes

Significant change in how the VAT rate is viewed with regard to elevator (lift) repairs

Judgment C-218/21 DSR of 5 May 2022 deals with a dispute between a company called DSR and the Portuguese tax authorities concerning the application of a reduced VAT rate to the repair and renovation of lifts located in residential buildings. The conclusion set forth in that judgment is based primarily on an interpretation of paragraph 2 of Annex IV to the VAT Directive, which, together with Article 106 of that directive, allows Member States to apply a reduced rate of VAT to repairs and renovations to private dwellings and residential buildings, with the exception of materials which form an essential part of the supply.

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The Portuguese company DSR produces lifts, hoists and conveyor belts and also provides lift repair and maintenance services. In 2007, DSR applied a reduced rate of VAT to the lift refitting and repair services supplied by it, while invoicing the materials incorporated in connection with those supplies at the standard rate of VAT. Following a tax inspection in 2011, the Portuguese tax authority found that DSR had wrongly applied the reduced rate of VAT to those services and stated that the basic VAT rate should have been applied to the complete supply (i.e. not only to materials but also to human labour).

DSR challenged the tax assessments with a lawsuit, which the Administrative and Tax

In the case of repairs and renovations of lifts in buildings not used exclusively for residential purposes, a mixed VAT rate is to be applied.

Court in Porto, Portugal initially upheld. It justified its decision on the grounds that the lifts are an integral part of the buildings in which they are located, and the application of the reduced VAT rate is therefore not precluded provided that the services in question are provided on the basis of a works contract and the reduced VAT rate is not applied to the materials which form a substantial part of these supplies, but only to the human labour. This condition is met by DSR.

The Portuguese tax authority appealed against this decision to the Supreme Administrative Court, which referred two requests for a preliminary ruling to the Court of Justice of the European Union (CJEU). The substance of the two requests for a preliminary ruling, which were examined together, was whether paragraph 2 of Annex IV to the VAT Directive must be interpreted as meaning that the term 'repair and renovation of private dwellings and dwelling houses' within the meaning of that provision includes services for the repair and renovation of lifts in residential buildings.

The CJEU stated that in order to meet the definition provided for in the above provision, it is necessary that the activity in question is actually repair or renovation, i.e. an activity characterised by its occasional nature, and not maintenance, which is, on the other hand, an activity carried out regularly and systematically (which is subject to the standard rate of VAT). Furthermore, it is necessary that the services provided relate to private dwellings or dwelling houses, i.e. immovable or movable property intended for private residence, and not to buildings used for commercial purposes, staff accommodation, hotels, etc.

Unlike the Portuguese tax authorities, the CJEU considers the common areas of exclusively residential buildings, where lifts are usually located, to be important, even essential, for the use of individual flats, and therefore the above provision also applies to the repair and renovation of lifts in residential buildings. However, in the case of repairs and renovations of lifts in multi-purpose buildings, i.e. those which are not only used as residential buildings but also for commercial purposes, for example, a mixed VAT rate should be applied (to apply the VAT rate, a pro rata apportionment should be made).

This of course raises the question of how to interpret the relevant provisions of the Czech VAT Act following this judgment.

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