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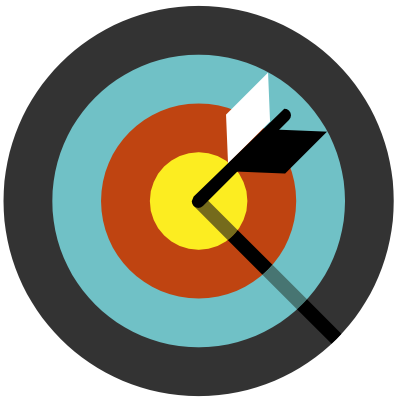
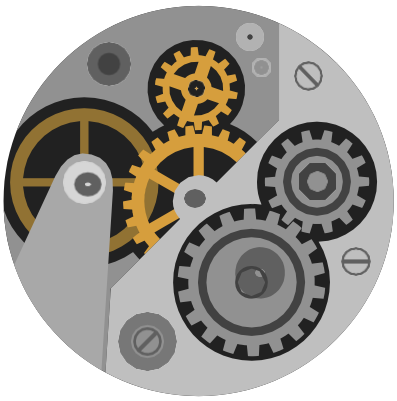


Accounting news



Tax news

Legal news

Grants & Incentives news

dReport: April 2018

Leaf through the regular overview of tax, legal and accounting news, get up to speed on subsidy and investment incentives developments.

Amendments to IFRS 2 endorsed for use in the EU

On 26 February 2018, Amendments to IFRS 2 Classification and Measurement of Share-based Payment Transactions were endorsed by the European Commission for use in the European Union. The EU effective date is the same as the IASB's effective date (annual periods beginning on or after 1 January 2018).

Amendments to IFRS 2 Share-based Payment that clarify the classification and measurement of share-based payment transactions were issued by the IASB in June 2016.

The amendments to IFRS 2 contain the following clarifications and amendments:

- The accounting for cash-settled share-based payment transactions that include a performance condition;
- The classification of share-based payment transactions with net settlement features;
- The accounting for modifications of share-based payment transactions from cash-settled to equity-settled.

More information about Amendments to IFRS 2 can be found in our Accounting Newsletter from September 2016.
The full version of the Amendments is available here.

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Amendments to IAS 40 endorsed for use in the EU

On 14 March 2018, Amendments to IAS 40 *Transfers of Investment Property* were endorsed by the European Commission for use in the European Union. The EU effective date is the same as the IASB's effective date (annual periods beginning on or after 1 January 2018).

The Amendments to IAS 40 were issued by the IASB in December 2016 to clarify transfers of property to, or from, investment property.

The amendments newly state that an entity shall transfer property to, or from, investment property when, and only when, there is evidence of a change in use. A change of use occurs if property meets, or ceases to meet, the definition of investment property. A change in the management's intentions for the use of property by itself does not constitute evidence of a change in use.

Examples of evidence of a change in use include:

a. commencement of owner-occupation, or of development with a view to owner-occupation;
b. commencement of development with a view to sale;
c. end of owner-occupation;
d. inception of an operating lease to another party.

An entity applies the amendments to changes in use that occur on or after the beginning of the annual reporting period in which the entity first applies the amendments. Retrospective application is also permitted if that is possible without the use of hindsight.

More information about Amendments to IAS 40 can be found in our Accounting Newsletter from January 2017. The full version of the Amendments is available here.

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IFRS EU Endorsement Process

The European Financial Reporting Advisory Group (EFRAG) updated its report showing the status of endorsement of each IFRS, including standards, interpretations, and amendments, most recently on 15 March 2018.
As of 25 March 2018, the following IASB pronouncements are awaiting European Commission endorsement for use in the EU:

Standards

- IFRS 14 *Regulatory Deferral Accounts* (issued in January 2014) - the European Commission has decided not to launch the endorsement process of this interim standard and to wait for the final standard
- IFRS 17 *Insurance contracts* (issued in May 2017)

Amendments

- Amendments to IFRS 9 *Prepayment Features with Negative Compensation* (issued in October 2017)
- Amendments to IFRS 10 and IAS 28 *Sale or Contribution of Assets between an Investor and its Associate or Joint* Venture (issued in September 2014)

- Amendments to IAS 19 *Plan Amendment, Curtailment or Settlement* (issued in February 2018)
- Amendments to IAS 28 *Long-term Interests in Associates and Joint Ventures* (issued in October 2017)
- *Annual Improvements to IFRS Standards 2015–2017 Cycle* (issued in December 2017)

Interpretation

- IFRIC 22 *Foreign Currency Transactions and Advance Consideration* (issued in December 2016)
- IFRIC 23 *Uncertainty over Income Tax Treatments* (issued in June 2017)

Click here for the Endorsement Status Report

US GAAP

Roadmap on non-GAAP measures issued by the CAQ

Are you preparing an annual report and hesitating if the non-GAAP information to be included is presented and calculated meaningfully?

The CAQ has issued a new publication advising on how to best handle the process preparation and approvals of the non-GAAP measures for US public companies and their audit committees. The general principles may, however, be found relevant and meaningful to any public company.

While the GAAP information provides a reliable basis for investors and other readers of the financial statements in respect to the company's performance, the non-GAAP financial measures are also becoming more and more important and valuable to the users.

Examples of such non-GAAP financial information may be:

- EBITDA,
- adjusted operating income,
- adjusted EPS,
- FFO (Funds from Operations) used in real estate industry and many others.

For the US public companies the non-GAAP measures are defined by the SEC (US Securities and Exchange Commission).

Published non-GAAP measures are key to users if prepared in a balanced and comparable way.

The Center for Audit Quality (CAQ) which is an autonomous, nonprofit public policy advocacy organization based in Washington, DC affiliated with the American Institute of CPAs, issued a Roadmap for Audit Committees in the area of non-GAAP measures in order to provide audit committees with suggestions, considerations and best practices to follow when assessing the non-GAAP information to be disclosed in order to get a balanced picture of the company.

The Roadmap can be found on the CAQ's webpage here.

Key considerations pointed out by the CAQ are among others:

- Suggest to try:
  - "Putting itself in the investor's shoes.."
  - "Asking management whether it has an internal policy ..."
  - "Discussing with management how the company makes changes to non-GAAP measures it presents...."
  - "Asking the company to compare or benchmark to the peers"
  - "Finding out what disclosure controls.... Are in place..."
  - "Consulting with external auditors on their responsibilities in the area, on their prospective and their views of the company's performance if consistent with the auditor's understanding and knowledge of the company".

Companies may as well consider involving external advisors and auditors to support them when implementing processes and policies related to preparation and review of non-GAAP measures.

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Categorisation of Reporting Entities Two Years Later

The extensive amendment to Act No. 563/1991 Coll., on Accounting, as amended (the "Accounting Act"), has introduced "categorisation of reporting entities", effective since 1 January 2016.

A more detailed classification should allow for more appropriate adjustment of obligations in the reporting and presentation of accounting information. Micro entities continue to be "protected" by the EU Directive and Member States are not allowed to increase the entities' administrative obligations. On the contrary, this does not apply to large entities from which a Member State may require, in justified cases, more information, more extensive reporting etc. Legislation defines minimum requirements for information to be disclosed in notes to the financial statements for various categories; however, it is at an entity's discretion to disclose more information than the required minimum.

Categorisation also relates to the statutory audit of financial statements.

Since 1 January 2016, new criteria have been applied to categorise reporting entities, whereby two criteria out of three have to be met in order to classify an entity within a category:

Reporting entity	Total assets (net)	Total annual turnover	Average headcount
Micro	Up to 9 million	Up to 18 million	Up to 10
Small	Up to 100 million	Up to 200 million	Up to 50
Medium -sized	Up to 500 million	Up to 1 billion	Up to 250
Large	Over 500 million	Over 1 billion	Over 250

Two years after the implementation of the Act, it has become relatively clear that the legislator required assets to be assessed using their net values. Let me just remind you that the definition of turnover is hidden at the very end of Appendices 2 and 3 to Regulation No. 500/2002 Coll., providing implementation guidance on certain provisions of the Accounting Act, as amended, for entities that are businesses maintaining double-entry accounting records ("Regulation"). The turnover is defined as the sum of Sales of goods + Sales of services + Other operating income + Income from non-current financial assets + Income from other non-current financial assets + Interest income + Other financial income.

In practice, however, we are often asked how to classify a specific reporting entity appropriately and when to change its category.

Section 1e of the Act stipulates that if a reporting entity exceeds or ceases to exceed two limit values under Sections 1b and 1c as of two subsequent balance sheet days of regular financial statements the reporting entity changes the category under which the scope and method of preparation of the financial statements is defined starting from the beginning of the immediately following reporting period.

The frequent source of incorrect classification or a premature change of the reporting entity's category is the inconspicuous interim provision of the Act stipulating how reporting entities are arranged on the starting line after the adoption of the amended Act and from which date the reporting periods are counted.

In the reporting period started in 2016, a reporting entity follows the legal regulations for a category of reporting entities and a category of groups of reporting entities the conditions of which were met as of the balance sheet date immediately preceding the reporting period.

This means that in the first year of the amendment application (ie in 2016), the requirements as of 31 December 2015 were applied and the reporting entity was categorised accordingly. The first classification is not included in the calculation of the "number of limit value excesses".

Example 1

	Total assets (net)	Total turnover	Number of employees	Reporting entity category
31 Dec 2015	300 000 000	17 000 000	12	Small
31 Dec 2016	455 600 000	240 000 000	20	Small (Medium-sized)
31 Dec 2017	460 000 000	250 000 000	49	Small (Medium-sized)
31 Dec 2018				Medium-sized

At the start (as of 1 January 2016), the reporting entity is classified as a "small" entity according to the results as of 31 December 2015. This first classification is not included in the number of periods in which the excess of limit values is monitored.

Even though the entity was doing well in the following two years and exceeded two limit values (assets and turnover) to be reclassified as "medium-sized" as of two subsequent balance sheet days, it continues to report as a small entity in 2016 and 2017. Only after exceeding two out of the three limit values in two subsequent years it starts reporting under another category, in our example as a medium-sized entity.

This consideration is not complex and most people reading the Act carefully enough will have no problem to apply it correctly.

Let us give you a more complicated example:

Example 2

	Total assets (net)	Total turnover	Number of employees	Reporting entity category
31 Dec 2015	500 000 000	12 000 000	18	Small
31 Dec 2016	800 000 000	650 000 000	137	Small (medium-sized)
31 Dec 2017	950 000 000	2 150 000 000	260	Small (large)
31 Dec 2018				Medium-sized

In this example, the reporting entity has grown rapidly. At the start, it was classified as "small" according to its results in 2015 and continued to report as "small" in 2016 and 2017.

As of the first tested balance sheet date on 31 December 2016, it exceeded two out of the three categories to become a "medium-sized" entity.

As of the second balance sheet date on 31 December 2017, it even achieved the values attributable to the "large" category.

It is obvious in this case that the reporting entity has to change its category in 2018; the question may be what classification is appropriate – is it a medium-sized or a large entity? The reporting entity exceeded two limit values for the "medium-sized" category as of two subsequent balance sheet dates of regular financial statements and the values for the "large" category as of the latter balance sheet date. In applying Section 1e of the Act, we have to come to the conclusion that the reporting entity exceeded limit values for the "medium-sized" category as of two balance sheet dates (for the "large" category only once) and thus in the 2018 reporting period it will report as a "medium-sized" entity.

In conclusion, there is the most interesting example:

Example 3

A small entity merges by amalgamation with a large entity. The small entity is the successor. If we strictly applied

the letter of the law we would come to the following conclusion:

- No establishment or start of activities under Section 1e occurred, ie the category of the reporting entity is not estimated and the original category of a "small" entity continues to apply.
- Two limit values were not exceeded under Sections 1b and 1c as of two subsequent balance sheet dates of regular financial statements, ie the category of the reporting entity will not be changed for two years.

The large entity that merged by amalgamation with the small entity thus becomes small with all of the advantages for financial statements presentation and other reporting.

We believe that such treatment would violate the correctness principle that prevents avoiding the purpose of the law. Section 8 (2) of the Act stipulates that accounting books are considered correct if maintained by the reporting entity in compliance with and without avoiding the purpose of the Act and other legal regulations. It is contrary to this principle if in fact a large entity takes advantages of small entity reporting through a formal transaction.

As stated at the beginning, the purpose of reporting entity categorisation is to determine the corresponding related obligations contained in other sections of the Act, or legal regulations directly relating to accounting, such as the Act on Auditors. Meeting relevant obligations is assumed by law starting from the establishment of an entity, or from the date on which the entity starts its activities. If the obligations are applicable to newly established entities or entities starting their activities the more they apply to entities that undergo transformations.

Although there is no doubt that the approach to similar transactions will be adjusted in practice over time we recommend changing the category in similar situations depending on the evidence available after the transformation in the financial statements for previous periods, taking into account the "substance over form" principle and in our example, we would change the category to "large".

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Inconspicuous amendments to the Income Tax Act

A brief summary of additional amendments to the Income Tax Act undergoing the legislative process

In our previous issues of the Tax dReport, we focused on the relatively extensive amendment to the Income Tax Act ("ITA") which is expected to introduce substantial changes to international taxation and other fields starting from 2019. We note that the amendment is just at the initial stage of the legislative process, with comments being now dealt with by the Ministry of Finance. We will keep you informed about any further development.

The amendment has rather overshadowed additional amendments to the ITA that are presently being debated in the Chamber of Deputies. Let us provide you with a summary of the proposed changes:

Proposed limitation of the 'basic investment fund' category

The Senate's amendment is part of the debate within the second reading in the Chamber of Deputies. With effect from 1 January 2019, it proposes narrowing the definition of the 'basic investment fund', which is subject to the more favourable five-percent rate treatment.

Restoring the expense charge-off flat rate for sole traders to the original level

Another amendment to the ITA is in the first reading, restoring the limits of expense charge-off flat rates to the level of 2016. Legislators state that the introduced reduction of expense charge-off flat rates has been incorporated to the bill through an amending motion and as such, the impact of the measure has not been assessed sufficiently. The administrative burden related to the registration of sales, local sales and purchases reporting and other governmental measures introduced for minor businesses and sole traders has increased and thus it would be appropriate not to expand administrative requirements in income taxation.

Taxation of financial compensation for the church

The amendment to the Act on Property Settlement with Churches and Religious Institutions (the "Act") comprises a related amendment to the ITA. With effect from 1 January 2019, the amendment proposes narrowing the existing provision on the subject of taxation to the extent that the income from gratuitous acquisition of property, except for financial compensation, under the Act by community service taxpayers is not subject to tax. All financial compensation paid out to churches and religious institutions would thus be subject to tax in the future.

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New Rules for Taxing Digital Companies

On Wednesday 21 March 2018, a proposed reform was presented, enabling member states of the European Union ("EU") to tax revenues generated by large digital companies in their territories. The proposal should thus eliminate the existing discrepancy between where the revenues are generated and where they are taxed. The proposal was strongly opposed by the United States of America as well some EU member states (such as Ireland and Luxembourg) that attract large firms with low taxes.

The reform is a response to the ongoing digital revolution where the rules for taxing digital companies operating in Europe are highly limited, namely owing to the existing definition of a permanent establishment. The original rules were drawn up in the previous century prior to the introduction of the Internet and were based on the assumption that cross-border trade is based on the physical import and export of goods and services. The existing setup thus makes it impossible for member states to tax digital companies operating in Europe unless they have a sufficiently large physical presence in the EU's territory.

The proposal works under the assumption that the calculation of the tax base would first be unified, with revenues generated by multinational corporations subsequently divided among all the countries where the company operates. The reform would **introduce the legal definition of a "digital presence"** of companies in the territories of member states for the purposes of corporate taxation. Thanks to this, it would be possible to tax companies in the territory of the given state without the company having a physical presence in it and with the company's digital activities playing the decisive role. Permanent establishments would be set up by the companies that met at least one of the following criteria: annual income from digital services in the given member state in excess of EUR 7 million, over 100 thousand users in the given state during the taxation period, or over 3 thousand contracts for the provision of digital services entered into with other firms during the taxation period.

According to the European Commission, the new rules should also address a fairer allocation of collected revenues among individual states based on the on-line value generated. The criteria could include, for example, the location

of the user at the time of using the service.

In adopting the proposal, legislators of individual member states will thus have to tackle the task of preventing double taxation. The rules for preventing double taxation are stipulated by double taxation treaties; however, the relevant provisions are outdated. A directive should prevail over international treaties concluded by EU member states; nevertheless, amendments to treaties would need to be negotiated with non-EU countries. As a matter of interest, approximately 60 treaties would need to be revised solely in the Czech Republic's case.

As the approval of the directive itself is expected to take some time, the EU has come up with a provisional solution whereby certain digital activities would be subject to "interim tax". This is a response to the activities of certain states (Italy, Slovakia and others) that have already approved or started to enforce similar measures. Although the proposed tax is classified as income tax, it would, in essence, consist of the indirect taxation of income from the sale of advertising space on the Internet, from digital mediation activities or from the sale of user data. The measure would apply to companies with a minimal global annual income of EUR 750 million, of which income from the EU should amount to no less than EUR 50 million. The measure would apply to both cross-border and domestic services (to prevent unlawful discrimination). At this point, it should be noted that the introduction of the interim tax could lead to double taxation both at the level of turnover taxation and the level of standard profit taxation.

At the expected rate of 3% of gross revenues (ie excluding costs, if any) from digital services, member states' annual income is estimated to increase by up to CZK 127 billion following the introduction of the tax.

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Indirect Taxes

Defending One's Tax-Related Rights Is Not a Losing Battle

Although in some cases defence against decisions and procedures of the Tax Administration of the Czech Republic may seem to be a lengthy battle with uncertain outcomes, the recent rulings of the Supreme Administrative Court ("SAC") often indicate the opposite. In early 2018, the SAC issued two crucial rulings substantially revising the tax authorities' practice and setting a positive direction towards taxable entities.

Both rulings of the SAC may be considered significant in terms of tax administration as well as positive for taxable entities. These rulings serve as a certain confirmation for taxable entities that bringing cases before the court does not have to be a losing game.

The first ruling (ruling of the SAC no. 5 Afs 60/2017 – 60) was issued in a case in which a company was denied a VAT deduction by the tax administrator due to the company's alleged involvement in a fraudulent scheme. The SAC subsequently cancelled the judgment of the court and the Appellate financial directorate's ruling because it was not clearly demonstrated that the company knew or could have known about its involvement in VAT fraud. The SAC predominantly criticised the purposive assessment of evidence when both administrative authorities emphasised the evidence counting against the company while disregarding the evidence that was to the company's benefit. The SAC believes that it is always solely the tax administrator's responsibility to demonstrate that the taxable entity knew or could have known about the fraudulent practices concerned. The burden of proof thus cannot be transferred to the taxable entity, nor is it possible to extend incommensurately the requirement for examining the business partners' credibility as indicated by the judgments of the Court of Justice of the European Union and to place inadequate requirements on taxable entities. The SAC also emphasised that taxable entities are unable to examine all potential sub-suppliers involved in a business transaction and thus it is impossible to automatically count against the taxable entity the fraudulent practices of entities other than direct business partners as this would establish liability without fault. On the other hand, the SAC gave a reminder of the rule that the taxable entity should be cautious when suppliers, subject of performance, price or other circumstances raise doubts as to the transaction credibility.

The other ruling (ruling of the SAC no. 5 Afs 78/2017 - 33) relates to the statutory duty to guarantee VAT not paid by the supplier. In the legal dispute in question, the company was invited by the tax administrator to settle as a guarantor the VAT underpayment arising from a debt that was unsuccessfully collected from the supplier as part of enforcement of a judgment by a licensed enforcement agent. The tax administrator believes that a guarantee obligation was established as the respective performance was paid by a VAT payer in a cashless transfer to the supplier's account maintained abroad (Slovakia). Nevertheless, the Regional Court cancelled the tax administrator's decision and this was

further confirmed by the SAC. The SAC stated that the tax administrator must bear the burden of proof, demonstrating that the taxable entity knew or could have known about the supplier's intention not to pay VAT. Furthermore, the SAC opines that as such, a cashless payment to a foreign bank account cannot establish a guarantee for the actions of another taxable entity that has failed to pay VAT. Besides, the SAC opines that cross-border payments are not unusual in business relations, complying with the principle of the free movement of capital in the European Economic Area.

Nevertheless, the SAC did not agree with the Regional Court's opinion that the legal title of guarantee is contrary to the law of the European Union.

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In Brief

The Upcoming Amendment to the VAT Act (Rate-Related)

As part of amendments to the Act on Electronic Sales Records, it has been proposed to significantly expand the application of the 10% VAT rate to include supplies and services that are currently subject to a 15% tax rate. Starting from 1 January 2019, the 10% VAT rate could thus apply to the provision of catering services, hairdressing and cosmetic services, shoe repairs or the supply of fresh-cut flowers.

Proposed Technical Amendment to the VAT Act

The upcoming amendment to the VAT Act that should, starting from 1 January 2019, revise rules for correcting the tax base, extend the possibility of reducing VAT in respect of irrecoverable receivables, introduce a new definition of finance leases and implement procedures for taxing single-purpose coupons, has been subject to external consultation. The Ministry of Finance will address the comments received in the coming weeks. Afterwards, the draft wording should be submitted for approval.

Judicature of the Court of Justice of the EU

In its ruling C-396/16 T-2, the Court of Justice (the "CJEU") commented on the obligation to proportionally decrease the VAT deduction claim if the debtor that is being reorganised is supposed to pay only a proportional part of the original amount of receivables. In addition, the CJEU considered whether there might be room for eliminating the obligation. The CJEU's ruling indicates that approaches to the issue may be diametrically different in individual EU member states subject to local insolvency regulations. In this context, it may be recalled that the Ministry of Finance of the Czech Republic is preparing an amendment to the VAT Act that should (without further doubt) make it possible to correct tax in respect of receivables from debtors that are being reorganised (and to reciprocally enforce the obligation for the debtor to correct the tax deduction).

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International TAX

Is Dutch legislation contrary to the Treaty on the EU?

On 22 February 2018, the First Chamber of the Court of Justice of the European Union ("CJEU") issued a ruling in joined cases C-398/16 and C-399/16. Both disputes concern compliance, or the lack thereof, of the Dutch legal treatment of limitations of deducting borrowing costs and exchange rate differences under certain conditions with Articles 49 and 54 of the Treaty on the Functioning of the European Union ("TFEU"), which stipulate the freedom of establishment of citizens of one member state in the territory of another member state. Although both disputes seemed similar at first glance and were therefore heard together, it is surprising that they were concluded with different results. While the Dutch legal provision applied in case C-398/16 was assessed as being contrary to Articles 49 and 54 of the TFEU, the provision applied in case C-399/16 was assessed as being compliant with the aforementioned articles.

The subject of the dispute in case C-398/16 was the **rejection of deductibility of interest** arising from a loan on the part of a Dutch parent company which used funds borrowed from a Swedish company in the same group to purchase an equity investment in an Italian subsidiary. Dutch law limits the deductibility of interest expenses and other related borrowing expenses arising from a loan that is legally or factually directly or indirectly payable to a related party or a related natural person, if this loan is connected to the acquisition or purchase of shares in profit, share certificates and membership rights in a related party. Nevertheless, the Dutch parent company still deducted the interest from its tax base and it was therefore issued an additional payment assessment.

However, the Dutch parent company filed a legal action against the additional payment assessment, stating that its freedom of establishment had been restricted, which is

contrary to the aforementioned Articles 49 and 54 of the TFEU, since if it had used the borrowed funds to purchase an equity investment in a subsidiary resident in the Netherlands, it could have created a single entity with this subsidiary for tax purposes (tax consolidation).

Dutch law allows the creation of a single unit for tax purposes to a parent company that owns at least a 95% holding in the paid-up share capital of another taxpayer (subsidiary) in the legal and economic sense. If this condition is met, it is possible upon request of both taxpayers to collect tax arising from income in the Netherlands in the same way as if they were just one taxpayer. Which, in other words, means that thanks to the consolidation, mutual relations arising from capital participation such as the parent company's capital investment in a subsidiary become tax natural within one tax entity.

The CJEU concluded this dispute by stating that the Dutch government has committed a difference in treatment that cannot be justified by the necessity to maintain the allocation of the power to impose taxes between the member states or the necessity to maintain the coherence of the Dutch tax system, and the applied procedure also cannot be justified as a prevention of abusive tax practices.

The second discussed dispute (C-399/16) concerned the rejection of deductibility of an exchange rate loss of a Dutch parent company arising from the revaluation of a holding in a subsidiary based in the United Kingdom. The reason is that Dutch legislation stipulates that determination of profit does not take into account income from an equity investment or expenses incurred with respect to the acquisition or transfer of this equity investment (this rule is also called the "holding exemption").

In this case the Dutch parent company likewise appealed against the additional payment assessment. The reason for filing the appeal was the parent company's belief that its freedom of establishment had been restricted, since if it held an equity investment in a company resident in the Netherlands, it could create a single entity for tax purposes with this subsidiary and all relations resulting from the capital participation in it would become non-existent for tax purposes thanks to the consolidation.

However, the actions of the Dutch government were assessed as being compliant with the freedom of establishment since the rules of the "holding exemption" stipulate that the increase or decrease in the value of the holding arising from exchange rate development of the foreign currency in which the value of the holding is denominated shall not be taken into account for profit determination purposes. This is the principal reason why the Dutch parent company could not deduct the exchange rate loss it incurred as a shareholder with respect to the value of its investment (subsidiary based in the United Kingdom) from its taxable profit. In the CJEU's opinion, a difference in treatment cannot be based on the assumption that if the Dutch company incurred a loss in relation to its holding in a subsidiary resident in the Netherlands, it could create a single taxpayer with the subsidiary and make this exchange rate difference tax neutral, because it is highly improbable that this holding would be denominated in a currency different from the one in which the company's profit is denominated.

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News round-up BEPS

Action 5 – Countering harmful tax practices more effectively, taking into account transparency and substance

Italy – On 6 February 2018, the Ministerial Decree of 28 November 2017 was published in Official Gazette No. 30 which enacts implementing rules for the patent box regime introduced by Law No. 190 of 23 December 2014. Under the patent box regime, 50% of income derived from the exploitation or direct use of qualifying IPs is exempt from corporate income tax and regional tax on productive activities. In addition, capital gains arising from the sale of qualifying IPs are not included in taxable income if at least 90% of the proceeds is reinvested, within the following two tax years, in R&D activities for the development, maintenance and improvement of other qualifying IPs.

Action 13 – Transfer pricing documentation and country-by-country reporting

OECD – the additional Guidance on the implementation of CbC Reporting was released on 8 February 2018. The Guidance addresses two specific issues: the definition of total consolidated group revenue and whether non-compliance with the confidentiality, appropriate use and consistency conditions constitutes systemic failure. The Guidance is available on the official website of OECD. A compilation of the approaches adopted by member jurisdictions of the Inclusive Framework was released on 28 February 2018. The Compilation document contains information about the approaches implemented by individual jurisdictions and defines the approaches that are permitted for CbC Reporting under BEPS Action 13. The Compilation document is available here.

Action 15 – Multilateral convention to implement tax treaty related measures to prevent BEPS

Czech Republic – On 14 February 2018, the Czech Republic's Cabinet approved the ratification of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI). The Czech Republic signed the MLI in Paris when it was opened for signature on 7 June 2017. The purpose of the MLI is to enable jurisdictions to swiftly implement the results of the BEPS project in more than 1,000 international tax treaties. At the time of signature, the Czech Republic submitted its provisional list of reservations and notifications and identified 87 treaties to which it intends to apply the MLI.

Slovenia - On 23 February 2018, Slovenia became the fifth jurisdiction to ratify the MLI. Slovenia is the fifth jurisdiction to ratify the MLI after Austria, Isle of Man, Jersey, and Poland. Once it deposits its ratification instrument with the OECD, the requirements for entry into force will have been met. According to article 34, the MLI will enter into force on the first day of the fourth month after the date on which the fifth jurisdiction deposits its ratification instrument. The MLI is expected to generally take effect in early 2019.

New joiners of the BEPS inclusive framework

The OECD announced on 19 February 2018 that Serbia joined the inclusive framework for the global implementation of the BEPS project. Under the inclusive framework, all OECD state and non-state jurisdictions that commit to the BEPS project will participate as BEPS associates of the OECD's Committee on Fiscal Affairs. Joining the BEPS inclusive framework means that Serbia must implement four minimum standards: countering harmful tax practices, preventing treaty abuse, transfer pricing documentation and enhancing dispute resolution. There now are 112 jurisdictions participating in the inclusive framework. The full list can be accessed on the OECD website.

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In Brief

Belgian constitutional court abolishes fairness tax

On 1 March 2018, Belgium's constitutional court rendered its long-awaited decision on the fairness tax. The fairness tax, which has applied since tax year 2014, is a separate tax imposed at a rate of 5.15% on dividend distributions by companies (other than small or medium-sized enterprises) to the extent that such companies offset taxable income in the year of the distribution with a current-year notional interest deduction (NID) and/or tax losses carried forward. The fairness tax is levied on both resident companies and permanent establishments (PEs) of foreign companies. In line with the CJEU decision, the constitutional court cancelled the fairness tax for resident companies that redistribute dividends, because of the incompatibility with the Parent Subsidiary Directive. Since the constitutional court's decision regarding the application of the tax to resident companies renders the fairness tax ineffective, the court decided to annul the regime in its entirety with an effect as from tax year 2019.

China publishes new rules on beneficial owners

On 3 February 2018, the State Administration of Taxation published new rules on the concept of a beneficial owner of income under China's tax treaties which will apply to tax payment or withholding obligations that arise on or after 1 April 2018.

Malta amends notional interest deduction rules

On 2 February 2018, Malta's Minister for Finance published new notional interest deduction (NID) rules 2018 to replace the rules introduced in 2017. The NID rules are designed to align Malta's tax treatment of debt and equity (i.e. interest on financing is a tax-deductible expense, while dividends are not deductible) and, therefore, bring equity financing on a par with debt financing. This alignment is achieved by allowing Malta companies and partnerships (including Malta permanent establishments of foreign companies or partnerships) to claim a deduction for "interest on risk capital." Specifically, such companies will be able to claim a deduction against their chargeable income for notional interest deemed to be incurred on their risk capital. The new rules are applicable for financial years ending on or after 1 January 2017.

EC conditionally approved Malta's tonnage tax regime

On 7 February 2018, the European Commission published the official text of its 19 December 2017 conditional approval of the regime for a period of 10 years under the EU state aid rules. As a result of its investigation, the commission concluded that a number of wide-ranging tax exemptions granted by the tonnage tax regime constituted state aid and requested Malta to: remove the possibility for pure financial institutions to benefit from the tonnage tax regime; ensure that the exemption from tax on capital gains arising from the sale or transfer of tonnage tax ships is limited to companies engaged in genuine shipping activities; remove the exemption from the tax on capital gains on shares in shipping companies for Maltese resident shareholders; and remove the exemptions from duty on documents and transfers.

EU publishes non-confidential version of Amazon state aid decision

The European Commission's reason for concluding that an advance pricing agreement granted by Luxembourg to Amazon in 2003 amounted to state aid was that the ruling did not follow principles later recommended by the OECD for allocating risk and intangible-related returns. The decision is available here.

Chile-UK treaty most favoured nation clause applies

On 28 February 2018, HM Revenue & Customs (HMRC) announced that the most-favoured nation (MFN) clause in the UK-Chile tax treaty applies as from 1 January 2017. The MFN clause was triggered by Chile's treaty with Japan, which provides for more favourable withholding tax rates on certain interest and royalty payments, and came into effect as from 1 January 2017. The net result of the revisions is that the withholding tax rate on interest payments is reduced from 15% or 5% to 4% in certain circumstances, with the default rate of 15% reducing to 10% as from 1 January 2019. The withholding tax rate on royalties is reduced to 2% (from 5%) on royalties paid for the use of, or the right to use, industrial, commercial or scientific equipment; otherwise, the rate is 10%.

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Some Types of Tax Savings to Be Disclosed

In 2018, final political consensus was achieved on the wording of the EU directive, which introduces the obligation to disclose, among other things, such cross-border arrangements, the ultimate goal or one of the main goals of which is achieving tax advantages.

The wording of the directive, which was passed on 13 March 2018, is seen as a "compromise wording", as the Council of the European Union did not ultimately adopt some of the relatively radical recommendations of the European Parliament. Despite this fact, for instance, the limited retroactive effectiveness of the directive was preserved. Thus, the disclosure obligation will also relate to all arrangements, the implementation of which will be commenced by the tax payers already on the day the directive is issued in the Official Bulletin of the EU (that is, as expected, already in 2018) or later.

The member states are obliged to transpose the directive into their legal systems to ensure that the new rules become effective on 1 July 2020, at the latest. Some states, however, have been preparing the relevant regulations to come into effect earlier.

Subject of Disclosure

The directive introduces a new disclosure obligation and subsequent automatic exchange of information among the EU member states for arrangements with the following features:

1. The arrangement has cross-border elements defined by the directive; and
2. The arrangement has some of the elements defined in the annex to the directive, and at the same time, the main or one of the main benefits of the arrangement involves gaining "expectable" tax benefits; of
3. The arrangement is of a specific type and has at least one of the elements set forth in the annex to the directive (eg certain elements related to transfer pricing or lack of clarity in terms of the beneficial owner).

Entities Obliged to Report Cross-Border Arrangements

- The disclosure obligation to the relevant tax administrator will principally apply to so-called '**intermediaries**'.
- The directive defines intermediaries as any person that designs, markets, organises or makes available for implementation or manages the implementation of a reportable cross-border arrangement. However, the disclosure obligation will be borne by all persons that knew or could have known that they undertook to provide direct or indirect support, help or advisory in respect of the above-defined activities related to cross-border arrangements.
- In the event that the intermediary is prevented from meeting the disclosure obligation due to its legal confidentiality obligation (which, in the Czech Republic, applies to tax advisors and attorneys-at-law), **the disclosure obligation shifts to the tax payer** who intends to benefit from the relevant arrangement.
- **The tax payer** will also bear the disclosure obligation in the following cases:
  1. In the event that no intermediary took part in the reported cross-border arrangement (eg if the tax payer creates the arrangement itself or with the help of a party that cannot be denoted as an intermediary); or
  2. In the event that the intermediary itself is not subject to the disclosure obligation (eg the intermediary provides its services completely outside the territories of the EU member states).
- The tax payer will also be obliged to submit information to the tax administrator on the utilisation of the relevant arrangement for every year in which the arrangement is applied.
- The member states will be obliged to define effective **sanctions** for non-compliance with the obligations set out by the directive.
- **Protection of good faith**: It will not be possible to impose penalties for non-compliance with the disclosure obligation on entities that prove that they did not know they were engaged in a cross-border arrangement to which the disclosure obligation applies.

Deadlines to Submit Reports

- Cross-border arrangements affected by the directive, the implementation of which commenced between the issuance of the directive in the Official Bulletin of the EU (the issuance of which is anticipated to take place already in 2018) and 1 July 2020 are to be reported by the relevant entities by 31 August 2020.
- In other cases, the reporting deadline is defined as 30 days (i) from the day on which the draft arrangement was prepared and the support, help or advisory therefor was provided, (ii) from the day on which the arrangement was prepared for implementation, or (iii) from the day on which the implementation of the arrangement began. The deadline start will be determined based on which of the events referred to above occurs earlier for the entity obliged to report.

Silence of the Tax Administrator Does not Mean Its Agreement

The directive explicitly states that the tax administrator's not responding to notifications does not automatically mean that it agrees with the reported cross-border arrangement.

Retroactive Effectiveness

The disclosure obligation also applies to cross-border arrangements, the implementation of which was commenced by the tax payers between the day the directive entered into force and the day it was effectively transposed into the legal systems of individual member states (ie by 1 July 2020, at the latest).

Automatic Exchange of Information among the Member States

The member states will automatically exchange the information collected as part of the compliance with the disclosure obligation. The first set of information is to be submitted by 31 October 2020.

We will discuss this topic also in our next webcast.

Do not hesitate to contact us if you would like to know in which scope the duties specified above will specifically apply to you.

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The Battle for Professional Secrecy is Over. Or is it…?

The proposed amendment to the Tax Code, about which we have already informed you, was, following heated debates, finally approved by the Chamber of Deputies of the Parliament on 21 March 2018.

The original proposal, which substantially exceeded the requirement of the directive on administrative cooperation in the field of taxation on which it should have been based, was, in the end, adopted in a relatively compromising form.

Provision of New Information to the Tax Administrator

Persons that are obliged to identify and check clients in line with the Act on Selected Measures against Legitimisation of Proceeds of Crime and Financing of Terrorism (the "AML Act") will newly be obliged to provide the tax administrator, at its request, with data obtained in identifying and checking the client as well as with documents obtained during the process that contain the information, and with information as to the method through which the information was obtained.

Protection of Professional Secrecy

However, only the General Financial Directorate (ie the central liaison office for international cooperation in tax administration) will be able to request the above stated information and documents from attorneys-at-law, notaries, tax advisors, judicial distraint officers and auditors, and it will only be able to do so for the purposes of international cooperation in tax administration. Said professionals will be obliged to provide the information under the same conditions and restrictions as in providing information to the Financial Analytical Office under the AML Act. In so doing, attorneys-at-law and notaries will, to a substantial degree, communicate through relevant professional chambers.

According to the transitory provision, the new obligation will additionally only apply to information that the above stated professionals obtained subsequent to its effective date.

The amendment is proposed to come into effect on the day that the act is promulgated in the Collection of Laws.

The transitory provision does not apply to persons liable under the AML Act that do not carry out one of the above stated professions, and the tax administrator will be allowed to contact them with a request for information at any time subject to the condition that the information is necessary for tax administration and that it cannot be obtained from the register maintained by the tax administrator or another public authority.

Breaking Banking Secrecy Restrictions

The amendment also extends the range of information that the tax administrator may request about clients of financial institutions or payment services providers.

The tax administrator will newly have the power to request details about unique identifiers connected with accounts, persons with the account handling authorisation, persons that deposited funds in the account, payment recipients, custody and leases of safety boxes.

The range of information that the tax administrator will be allowed to request from banks and other payment services providers no longer includes information about e-banking (eg the IP address or the phone number of the device used).

In justified cases and subject to statutory conditions being met, public authorities other than tax administration bodies that the law designates as tax administrators will also be able to request information.

More details about the changes will be provided in our upcoming webcastu.

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Tax liabilities – April 2018

April		
Tuesday, 3	Income tax	Submission of special-rate withholding tax settlement for February 2018
		Submission of special-rate withholding tax form settlement for tax year 2017
		Submission of tax return and payment of tax for 2017, if the taxpayer wasn´t required an audit and fills the tax return himself/herself
Monday, 9	Consumption tax	Tax maturity for February 2018 (except the consumption tax on alcohol)
Monday, 16	Road tax	Advance payment of tax for 1st quarter 2018
	Intrastat	The Intrastat statement for March 2018, paper version
Wednesday, 18	Intrastat	The Intrastat statement for March 2018, electronic version
Friday, 20	Value added tax	Tax return and maturity of the MOSS VAT
	Income tax	Monthly payment of deducted advance payments on personal income tax from employment
Tuesday, 24	Consumption tax	Tax maturity for February 2018 (only the consumption tax on alcohol)
Wednesday, 25	Lotteries and other similar games	Submission of statement for advanced payment on deduction from lotteries and other similar games and payment of advanced for 1. quarter 2018
	Value added tax	Tax return and tax for Q1 and March 2018
		EC Sales List, Q1 and March 2018
		VAT control statement for 1Q and March 2018
	Energy taxes	Tax return and tax maturity on gas, solid fuels and electricity for March 2018
	Consumption tax	Tax return for March 2018
		Tax return for claiming of refund of consumption tax for example on fuel oil and other petrol (benzine) for March 2018 (if applicable)
Monday, 30	Income tax	Submission of special-rate withholding tax settlement for March 2018

Tax liabilities – May 2018

May		
Thursday, 10	Consumption tax	Tax maturity for March 2018 (except the consumption tax on alcohol)
Wednesday, 16	Intrastat	The Intrastat statement for April 2018, paper version
Friday, 18	Intrastat	The Intrastat statement for April 2018, electronic version
Monday, 21	Income tax	Monthly payment of deducted advance payments on personal income tax from employment
Friday, 25	Value added tax	Tax return and tax for April 2018
		EC Sales List for April 2018
		Tax control statement for April 2018
	Energy taxes	Tax return and tax maturity on gas, solid fuels and electricity for April 2018
	Consumption tax	Tax maturity for March 2018 (only the consumption tax on alcohol)
		Tax return for April 2018
		Tax return for claiming of refund of consumption tax, for example on fuel oil, other petrol (benzine) for April 2018 (if applicable)
Thursday, 31	Real estate tax	Full tax maturity (tax payers with tax liability to CZK 5,000; including)
		Tax maturity of 1. tax payment (tax payers with tax greater then CZK 5,000 (excluding taxpayers engaged in agricultural production and fish farming)
	Income tax	Payment of special-rate withholding tax for April 2018

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GDPR: The Mystery Regarding the Personal Data Retention Period to Be Resolved by the GDPR Detective

The Detective was assigned to a new case. The Detective needs to resolve whether company ABC which processes e-mail addresses to send marketing offers does not retain personal data too long. Is the company prepared for the changes to be introduced in May 2018? What are the measures which the company needs to take to meet the GDPR requirements? Can your company identify with this mystery?

To ensure that the company is in line with the **GDPR (General Data Protection Regulation)**, it must be able to assess for how long personal data are to be retained. Personal data also include (among other things) e-mail addresses, which are handled by company ABC.

Why are e-mail addresses processed by ABC?

- To send marketing offers;
- To contact clients as regards the provision of services arising from concluded contracts; and
- To protect legitimate interests of the company (for the necessary period, the company retains the originals of concluded contracts with its customers including an e-mail address due to the potential risk of legal disputes).

The Detective knows that in this case the main lead relates to the "**storage limitation principle**". Under this principal, personal data may only be **retained for a period necessary for processing for the given purpose**. If there are not any data retention periods set after the expiry of which personal data must be deleted or anonymised, the personal data controller must **determine the rules for retaining such data, independently for each purpose of processing**. If the personal data in question are processed for multiple purposes, it is possible to retain them until the longest retention period has expired.

Three pieces of advice from the GDPR Detective: measures to be taken in your company as well:

1. For each purpose of processing, determine the period over which it is required to process personal data for the purpose in question. In particular, this period is to be found in legal regulations, rulings of authorities, standards, and recommendations of authorities as regards personal data protection.
2. Set up your processes and systems to ensure that the relevant personal data are always erased, automatically or manually, after the expiry of the respective period.
3. Please note that personal data erasure means erasing all forms of the data in question, that is not only from IT systems but also, for example, the physical shredding of documents.

Company ABC already has an idea of how it should handle the period of personal data retention. After seeing the detective, it has decided that...

- Marketing offers will be sent for one year from terminating the contractual relationship between the company and the respective client (this will be adjusted in consents to personal data processing).
- With regard to the services provided under a contractual arrangement, clients will be contacted over the contractual relationship between the company and the respective client, not in subsequent periods.
- The originals of contracts with clients will be retained by the company for 10 years after the contractual relationship between the company and the respective client has been terminated which corresponds to the statute of limitations in respect of all potential claims arising from the contract.

Are you seeking a solution to a similar or entirely different case? Why don't you make an appointment with the Detective and order our online application GDPR Detective. Our private eye will resolve personal data protection mysteries for you!

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The Act of the Year 2017 is coming to an end, you can only cast your vote until the end of March: In the 9th annual survey, we are selecting regulations with a positive impact on the Czech environment. You can select from six legal regulations. Which one is your favourite? Please note that you can only participate in the survey until the end of March.

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If you are interested in obtaining additional information regarding the services provided by Deloitte Czech Republic, please contact our legal specialists:

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Publishing a Call under the Operational Programme Environment (OPE) to Prevent Municipality and Industrial Waste

Under the OP Environment 2014-2020, a call was published within priority axis 3 "Waste management and material flows, environmental burden and risks" focusing on waste prevention. Eligible applicants involve public as well as business entities. Projects must be realised in the Czech Republic.

Objective of the call:

- Decreasing the volume of waste from production;
- Re-using products at the end of their lifetime; and
- Supporting the launch of the "door-to-door" system.

Support is intended for projects focusing on municipality and industrial waste prevention, such as:

- Establishing a collection network of containers for used textile goods;
- Establishing centres or systems for product re-use or food warehouse network; and
- Implementing technology to decrease the amount of produced waste.

The maximum aid intensity per project amounts up to 85% of aggregate eligible project costs. The minimum eligible realisation expenses amount to CZK 500 thousand (net of VAT).

Period for sending applications: 3 April – 31 July 2018

Announcement of the 3rd Public Tender under the GAMA programme

In early March 2018, the Technology Agency of the Czech Republic published the 3rd public tender supporting applied research, experimental development and innovations within the GAMA programme, sub-programme 2 (Seal of Excellence). The programme aims to support projects enabling the commercialisation of research outcomes.

Applicants include small and medium-sized businesses based in the Czech Republic which obtained the Seal of Excellence EK in SME Instrument (phase 1) within the 4th deadline of 2017 and the 1st deadline of 2018.

The maximum aid intensity per project amounts up to 55% of aggregate eligible project costs. The minimum eligible realisation expenses amount to EUR 39,286.

Eligible costs include personnel costs, costs of sub-supplies and other direct costs.

Period for sending applications: 8 March – 19 April 2018

Announcement of the 1st Public Tender of the National Competence Centre Programme

The Technology Agency of the Czech Republic intends to announce the 1st public tender within the National Competence Centre programme on **Wednesday, 28 March 2018**.
Main applicants include solely research organisations. Businesses – legal persons and individuals may participate as secondary applicants.

Main objective of the programme:

- Supporting projects aimed at increasing the efficiency and quality of the outcomes of applied research and technology transfer;
- Increased competitiveness of businesses; and
- Strengthening the excellence and application relevance of research organisations.

The maximum aid intensity per project amounts up to 80%.

Period for sending applications: 29 March – 31 May 2018

Contacts

If these issues relate to your company, we would be happy to provide you with more detailed information.
Feel free to contact us at any time

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