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dReport: May 2018

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R&D Tax Deduction

Regional Court: Clinical Trials of Medicaments Classified as Research

We would like to provide additional information on legal disputes concerning R&D deductible items, this time in the area of clinical studies. in late February, the Regional Court in Hradec Králové issued new judgments cancelling the ruling of the Appellate Financial Directorate (the "AFD"). Below is a summary of the ey findings.

The Company won two legal disputes with the AFD pursuant to judgments 31 Af 53/2016 - 52 and 31 Af 52/2016 – 60. The Company sought the cancellation of the ruling whereby the AFD rejected the Company's appeal against additional corporate income tax payment assessments for the taxation periods of 2011, 2012, 2013 and 2014 whereby the assessments were confirmed. The subject matter of the dispute included the AFD's ruling stating that the Company did not carry out research and development in line with Section 34 (4) of the Income Taxes Act.

The Company is a registered medical facility conducting clinical studies predominantly of phase III, ie systematic testing of medicaments on patients to demonstrate and verify the healing powers of the medicament and identify side effects. This includes the testing of already-developed medicaments following the completion of clinical testing phases I and II, according to the assignments of the Company's clients.

The AFD concluded that the Company had been engaged in an activity classified as the provision of services to a third party without own research as it only recorded the results of individual patients included in the project in relation to the administered medicaments. Moreover, the AFD believes that the administered medicaments did not represent an outcome of the Company's research and development activities and, as a result, this service did not include the element of own research. The AFD thus concluded that the Company's activities in the respective projects did not include an appreciable element of novelty and the Company was not exposed to the risk and uncertainty arising from research and development.

Nevertheless, the Regional Court did not agree with this conclusion and confirmed the Company's opinion that the activity in an R&D project consisted of seeking new findings regarding the effectiveness of medication and was performed by qualified professionals, which brought new findings on the healing powers of the respective medicament. What is more, the Regional Court also agreed with the Company's opinion that as such, the Company's performance of medical research entails the risk of failure of such research. This risk lies in the fact that it may come out during the clinical study that the testing practitioner incorrectly assessed the effects of administered medicaments and, as a consequence, failed to identify the danger for human health.

Therefore, the Company is not engaged in a mere routine activity solely including the record-taking of the results. The Regional Court believes that the Company's activities met the definition of research and development.

The Regional Court observed an unlawful assessment of the matter by the AFD in terms of substantive law and returned the case for further proceedings. The AFD subsequently filed a cassation complaint against the judgment at the Supreme Administrative Court. **This judgment is one of the few judgments at the level of regional courts which agreed with the taxable entity, observing that the definition of R&D activities and costs reported in a tax return was met.**

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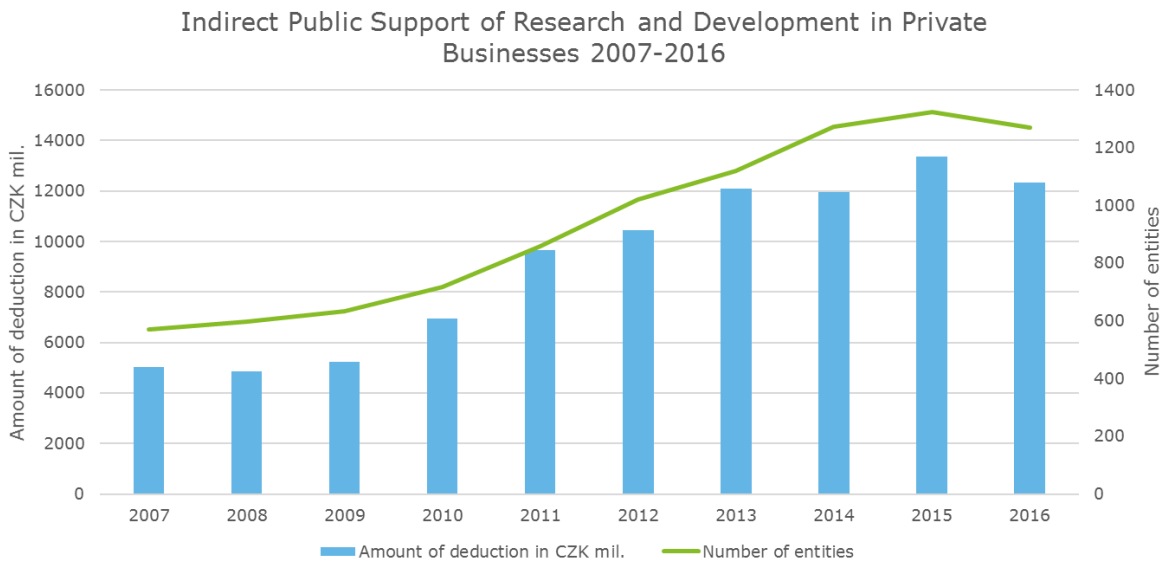
Current Trends in the Area of Deduction

As we have informed you in previous articles, R&D tax deductions are increasingly more often examined by the tax administration. The growing number of audits, which often result in legal disputes, leads to uncertainty among taxpayers. It is therefore questionable whether the setup of the deduction aimed at supporting research and development is the only accurate solution and whether it is time to consider an adjustment thereto, also considering the fact that the area has not been modified since 2005.

A decrease in the number of entities using the R&D tax deduction between 2015 and 2016 as well as a decrease in the aggregate costs reported by businesses as part of the R&D tax deduction in the same period proves the growing uncertainty among companies engaged in research and development in the Czech Republic arising from the tax administration's approach to the audit of tax deductions. This is alarming especially due to the fact that the decrease was recorded for the first time since 2005 when the R&D tax deduction was incorporated into legislation and also with regard to the boom in the Czech economy at present.

The figure below clearly depicts the statistics of applying the R&D tax deduction using the data of the Czech Statistical Office.



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Amount of deduction in CZK mil.	5 017	4 857	5 246	6 931	9 665	10 435	12 090	11 954	13 351	12 337
Number of entities	570	596	632	716	859	1 021	1 120	1 271	1 322	1 268

Source: Czech Statistical Office

We consider it problematic that formal project elements are currently preferred to the fact whether the company conducts research and development. Rather contradictory statutory requirements placed upon the research and development project documentation pose another issue. This includes, on one hand, the definition and approval of research and development activities prior to their commencement when the taxpayer does not (and cannot) have detailed solution descriptions as well as a sufficiently accurate and detailed definition of activities, including their timing, budget, staffing etc, on the other hand.

The current setting and practice bring about a great deal of uncertainty and disputes regarding the project commencement, factual definition of project activities and the onset or clarification of research and technical uncertainty.

Inspiration for potential changes in the setup of R&D deduction may be found abroad. in many countries having the R&D deduction in place, R&D projects are only processed retrospectively, subsequent to the termination of the respective taxation period and the relevant development task. This change could resolve persistent disputes between businesses and the tax administration concerning the definition of the term "project solution commencement". Furthermore, it could enable tax payers to specify in greater detail how exactly project activities were realised in the respective period which could ultimately be beneficial for the tax administration in assessing eligible activities.

The latest information indicates that the financial administration is considering certain changes in the setup of R&D deductions. Let us hope that these changes will support research and development in the Czech Republic, contribute to the more-transparent assessment of R&D activities and direct attention to the actual substance of the issue rather than to the fact whether or not companies are really engaged in research and development. Greater transparency in R&D deduction is important for both companies operating in the Czech Republic and businesses considering the establishment of new or expanding existing R&D centres in the CE region and contemplating in which CE country the centre should be located. The transparency of individual support regimes in the relevant countries is one of the key factors in this decision-making process which is crucial for whether or not the Czech Republic will be selected.

In view of the Czech Republic's efforts to support primarily investments with high added value, it should be essential for all of us that the R&D deduction setup become more transparent for businesses.

We will keep you updated on further developments in future dReport issues.

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In Brief

Judicature of the Court of Justice of the EU (CJEU)

Ruling C-8/17 Biosafe related to the application of a VAT deduction claim which was reported additionally based on a corrective tax document. Originally, the payment provided by a supplier was billed at a reduced tax rate; however, the supplier subsequently corrected the VAT rate replacing it with the standard one but it did so only after the period for applying the VAT deduction that started on the date of issuing the original invoice had expired. The CJEU stated that a period to deduct the additionally reported tax cannot start before the relevant corrective tax document is available to the relevant taxpayer. This opinion is in conflict with the VAT Act and has a high potential to change the practice in applying the Act.

Judicature of the Supreme Administrative Court (SAC) relating to the distraining of payment security orders

In its ruling 6 Afs 399/2017-26, the SAC has once again clarified the role that payment security orders may have in tax administration. It shows that a receivable arising from a distress warrant may be distrained for a time longer than the Financial Administration of the Czech Republic considered to be possible. This ruling is more developed in the article *Courts Have Once Again Sided with Entrepreneurs in Respect of Payment Security Orders*.

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OECD's Multilateral Convention Coming into Force on 1 July 2018

According to the latest information provided by the OECD, the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (the "Convention") will come into force on 1 July 2018.

As we have informed you in previous dReport issues, the Convention aims to implement unified rules preventing double taxation without the need for lengthy and complicated bilateral negotiations. Let us add that approximately 1,200 double taxation treaties are currently concluded across the world.

Ángel Gurría, the Secretary-General of the OECD, believes that the Convention will ensure that multinational companies will settle tax liabilities arising from their cross-border activities as appropriate.

The fact that the Convention will come into force after a mere year from the signing date is an indication of a strong political engagement in combatting base erosion and profit shifting (BEPS).

The Convention coming into force is based on ratification instruments deposited by five jurisdictions. Slovenia was the last jurisdiction to do so, on 22 March 2018. Ratification instruments had already been provided by Austria (22 September 2017), Isle of Man (19 October 2017), Jersey (15 December 2017) and Poland (23 January 2018).

The provisions of the Convention concerning withholding tax will take effect in the above-listed jurisdictions for all double taxation treaties concluded by these countries from the beginning of 2019. For other areas, the Convention will become effective within 12 months from coming into force, ie as of 1 July 2019 in the countries listed above. The Convention generally stipulates that provisions regulating the taxation of passive income will always take effect within six months from the Convention going into force while a 12-month period will apply to other provisions.

In other countries, the Convention will come into force within three months after these countries have deposited their ratification instruments. The information on how the ratification instruments have been signed and whether individual OECD countries have already signed them as of 22 March 2018 is available here.

Furthermore, the Convention will also introduce unified rules for handling hybrid mismatch arrangements, rules for defining permanent establishments and allocating profit to the permanent establishment as well as unified rules preventing the misuse of double taxation treaties. The Convention also includes a measure for addressing contractual disputes based on mandatory arbitration which was adopted by 28 signatories.

The Convention has not yet been ratified by the Czech Republic. Note that in the signing of the Convention, the Czech Republic reserved a right to introduce only minimum standards. in practice, a new preamble will apply in addition to Article 6 stipulating that the double taxation treaties aim to prevent double taxation as well as tax evasion as regards income and capital taxes. What is more, a possibility of restricting the advantages arising from individual treaties in case of their misuse is to be explicitly stated in Article 7. Improvements of problem resolution mechanisms for disputes concerning double taxation are newly specified in Article 16.

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New treaty with Turkmenistan

Implementation of the new Double Taxation Treaty with Turkmenistan will start on 1 January 2019

On 27 March 2018, the Double Taxation Treaty between the Czech Republic and Turkmenistan came into force. The wording of the Treaty is expected to be published in the Collection of International Treaties shortly. The provisions of the Treaty should be applied as follows:

- In respect of income and property taxes, the Treaty will be applied to income paid or credited as of 1 January 2019 or later.
- In respect of withholding tax, the Treaty will be applied to income paid or credited as of 1 January 2019 or later.

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News round-up BEPS

Action 2 – Neutralising the effects of hybrid mismatch arrangements

Australia – On 7 March 2018, the Australian government issued revised exposure draft (ED) legislation that incorporates the ED legislation released in 2017, as well as new rules to address branch mismatch arrangements and to introduce an integrity rule, which goes beyond the anti-hybrid rule recommendations of the OECD framework.

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

Luxembourg - On 22 March 2018, the Luxembourg parliament passed a law to replace the intellectual property (IP) box regime that was abolished in 2016. The law introduces a new article 50ter into the Income Tax Law (ITL) that provides for an 80% exemption on income derived from the commercialisation of certain IP rights, as well as a 100% exemption from net wealth tax (NWT). The new rules are expected to be applicable as from fiscal year 2018, once the necessary legislative steps have been completed, although it still is unclear when the Council of State will initiate the next steps to finalise the law so it can become effective.

Action 7 – Preventing the artificial avoidance of permanent establishment status

On 22 March 2018, the OECD released Additional Guidance on the Attribution of Profits to Permanent Establishments, a report that provides guidance mandated under the final BEPS action 7 report published in 2015. The newly released report contains additional guidance on the attribution of profits to permanent establishments (PEs) resulting from the recommended changes in the 2015 report to the definition of a PE in article 5 of the OECD model tax treaty.
The additional guidance follows on from two earlier discussion drafts issued in 2016 and sets out high-level general principles for the attribution of profits to PEs arising under article 5(5) of the model treaty, and includes examples of a commissionaire structure for the sale of goods and an online advertising sales structure and a procurement structure, and an example on the attribution of profits to PEs arising under the anti-fragmentation rule. The report also includes additional guidance related to PEs created as a result of the changes to article 5(4), and provides an example on the attribution of profits to PEs arising from the anti-fragmentation rule included in article 5(4.1).

Action 14 – Making dispute resolution mechanisms more effective

OECD – on 12 March 2018, the OECD announced the release of the third round of peer reviews on the implementation of the BEPS minimum standard on improving tax dispute resolution. A document addressing the implementation of best practices is also available on each jurisdiction that chose to opt to have such best practices assessed. These eight reports contain over 215 specific recommendations relating to the minimum standard. in stage 2 of the peer review process, each jurisdiction's effort to address the recommendations identified in its stage 1 peer review report will be assessed.

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In Brief

ECOFIN agrees on tax intermediaries directive

On 13 March 2018, EU finance ministers reached political agreement on the tax intermediaries directive proposed by the European Commission on 21 June 2017 that would require mandatory reporting by tax intermediaries and the automatic exchange of information by the tax authorities of member states for certain cross-border arrangements in relation to individuals, companies and other entities. The directive, which takes the form of an amendment to the Directive for Administrative Cooperation (DAC), is part of the efforts to tackle tax abuse and ensure fairer taxation in the EU, and broadly reflects the elements of action 12 of the BEPS project on the mandatory disclosure of potentially aggressive tax planning arrangements. The directive will be formally adopted during the next EU council meeting on 25 May 2018, and once adopted generally will apply as from 1 July 2020, with limited retroactive effect.

EU list of non-cooperative tax jurisdictions

On 8 March 2018, the EU's list of non-cooperative jurisdictions in taxation matters has been adjusted in the light of commitments made by listed jurisdictions and assessment of jurisdictions for which no listing decision had yet been taken. The Council removed Bahrain, the Marshall Islands and Saint Lucia from the list and added the Bahamas, Saint Kitts and Nevis and the US Virgin Islands. The adjusted list is available here. The EU has also published letters to potentially non-cooperative jurisdictions setting out the commitments required in the context of the preparation of the original list. The full version of letters is available here.

French ruling that Irish digital services provider has no PE in France

On 1 March 2018, the Paris Administrative Court of Appeal ruled that Irish-resident company Conversant International Ltd, which provides digital marketing services in France with the assistance of a French sister company, does not have a permanent establishment (PE) in France and is therefore not taxable in that country. The decision is based on the following arguments: Valueclick International Ltd did not have a PE in France within the meaning of article 2(9) of the France - Ireland Income Tax Treaty (1968) since the French sister company was neither a fixed place of business to the extent that all the services it provided were covered by the intercompany services agreement, nor a dependent agent of Valueclick International Ltd in so far as the French company was not authorised to conclude contracts in the name of Valueclick International Ltd.

New France-Luxembourg treaty signed

On 20 March 2018, the governments of Luxembourg and France signed a new tax treaty and protocol to modernise the existing agreement between the two countries, which now is 60 years old. The new treaty completely revamps the 1958 treaty and includes provisions that reflect the latest international standards found in the 2017 version of the OECD model treaty and recommendations under the BEPS project, as well as the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI).

Danish draft bill would end retroactive merger provision

Companies in Denmark that engage in cross-border mergers will no longer be entitled to retroactive effective dates for the mergers under a proposal by Danish Minister of Taxation. The amendment of the Merger Tax Act introduces a rule based on which any merger involving a Danish company cannot be considered effective in Denmark before the date of the merger agreement, according to a release from the tax authority. If adopted by the parliament, the new law will have an effective date of 23 March 2018.

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Courts Have Once Again Sided with Entrepreneurs in Respect of Payment Security Orders

The Supreme Administrative Court has again confirmed that it makes sense to defend yourself against the practices of the financial administration. in its latest ruling on the AB Chemitrans case, the court ruled that tax or related accrued interest and fees can only be recovered by distraint after the appellate proceedings have been concluded, which also applies to situations where the tax was subject to a payment security order. The ruling may significantly affect the existing practices relating to payment security orders and the performance of tax distraints.

In general, it applies that if the tax authority makes an additional tax assessment based on a tax audit, the additionally assessed tax is payable within 15 days of the delivery of the ruling on the appeal. Therefore, the tax authority is not allowed to collect the tax until after the appellate proceedings have ended when the payment assessment comes into force. However, if the tax is secured by a payment security order in advance, the tax authority has so far believed that the additional payment assessment may constitute grounds for a tax distraint as early as on the date it is delivered, ie regardless of the appeal filed. At that moment, the payment security order ceases to be effective, with the tax authority proceeding to perform the distraint and recovering the tax payable based on a payment assessment. However, in its latest ruling on the case of the Moravian company AB Chemitrans, the Supreme Administrative Court ruled that additionally assessment tax may only be recovered by distraint until after the appellate proceedings have ended with legal effect, which also applies to situations where a payment security order has been issued in the case in hand.

The legal opinion may have several practical implications. First, it may be inferred that payment security orders do not cease to be effective until after the appellate proceedings have ended with legal effect. Therefore, if, in the meantime, the appellate body or court revokes the payment security order for unlawfulness, the tax authority will be forced to refund the secured amount. The ruling may also affect the unlawfulness of the tax distraints already underway. in this regard, the issue of interest on unlawful acts, which the tax authority should pay to companies in situations like these, will also come into play.

Would you like to learn more about the ruling and its practical implications? Are you interested in the views of a Supreme Administrative Court judge on the latest tax issues? Would you like to know what tax issues are currently being addressed and how to prepare for them? Please accept our invitation to the seminar "It makes sense to defend yourself" to be held on 21 May 2018 with the participation of Mr Karel Šimka, a Supreme Administrative Court judge. To view the details about the event, follow this link.

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News in Immigration

Changes in the Ukraine Regime Project

The Ukraine regime was officially launched in August 2016. The Ukraine regime simplifies the hiring of employees from this country. It is intended for direct employers operating in the Czech Republic in the field of production, services or the public sector. Temporary help from Ukraine can help bridge the time when the Czech Republic's unemployment rate is critically low and companies currently lack 240,000 workers.

- Starting from 1 May 2018, the quotas will increase from 9,600 applications per year, i.e. 800 applications per month, to 19,600 applications per year, i.e. 1,600 applications per month (family members are not included in the quota).
- When filing a collective application for 50 or more people, it has been required since 1 February 2018 to demonstrate that the intention has been discussed with current employees and that approval of the mayor of the municipality where the foreigners will be accommodated after arriving in the Czech Republic has been obtained.
- As part of the increase in the number of accepted applications in the Ukraine regime, there is a concurrent increase in the capacities by the Ministry of Foreign Affairs at the Czech Consulate in Lviv.
- **Starting from 1 May 2018, applications for employee cards will be filed via the Lviv visa centre. The** visa centre will be created following the increase in the Ukraine regime quota. At present, a selection process for the external provider of the visa centre services is being conducted. Applications filed via the visa centre will entail a new fee for application processing. The fee is not expected to exceed EUR 20.

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The Mongolia Regime and the Philippines Regime

Other special programmes are intended to provide companies with temporary help to overcome the period of lack of employees. The Mongolia and Philippines regimes has been introduced with effect from 1 May 2018. They focus on countries whose labour force has continuously been a centre of interest of Czech employers.

The regime as such should serve for targeted and selective acceptance and processing of applications for employee cards by citizens of Mongolia and the Philippines who will perform work activities in the Czech Republic in the area of production, services or the public sector (on job positions CZ ISCO 4-8).

- The targeted and selective nature means that similarly to the Ukraine regime, the other states regime can include only a specific employer that meets the regime's criteria, together with a specific future employee or employees.
- Decisions on the applications for inclusion in the regime will be made by the Ministry of Industry and Trade (MIT) based on a recommendation from the Czech business representation or the CzechInvest Investment and Business Development Agency. The annual capacity for this project is 1,000 applications from each of the above countries (i.e. approximately 85 applicants per month per each country).
- Employee card applications will be accepted by embassies in Ulaanbaatar and Manila. After the monthly capacity of the respective embassies is filled, application acceptance will be suspended. Unlike the Ukraine regime, applications for the other country regime will not be put in an endless line. The applicants will be able to register several weeks in advance.
- The regime is intended only for direct employers that have been active in the Czech Republic for at least two years in the area of production, services and the public sector, that employ at least 10 people, have no payables to the state and have been persistently unable to fill an available job position from Czech labour market resources. The job position where the applicant included in the regime by the employer would be employed must correspond to the employer's business activity.
- The regime also allows filing a "collective application" for 30 or more applicants, with the employer having to complement the application with a sworn statement that it will cooperate with the Centres for the Support of the Integration of Foreigners in the region, a sworn statement about having discussed the intention with employees in line with Section 280 (1) of Act No. 262/2006 Coll., Labour Code, and a statement of the mayor of the municipality where the foreigners will be accommodated after arriving in the Czech Republic.

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Changes of conditions for filing an employee card application in Lviv

More than three quarters of Ukrainian employee card applicants are accepted via the government project. The Ministry of Foreign Affairs of the Czech Republic decided to end the so-called live queue and to introduce instead electronic registration via a dedicated e-mail address. All citizens can make a request for assigning a date in this way on their own and free of charge. One of the main reasons for this new setup was to eliminate intermediaries who abused the existing system. The registration does not take place via the Consulate General but via the Ministry of Foreign Affairs headquarters, so that the Consulate General cannot be accused of changing the order.

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Transposition of the EU directive

The reports on the transposition of Directive 2004/114/EC and Directive 2005/71/EC showed a variety of flaws and the need to perform several changes. For the sake of clarity, the EU decided to rework both directives and replace them with a new one.

For this reason, the European Parliament and the Council approved on 11 May 2016 Directive 2016/801/EU on the conditions of entry and residence of third-country nationals for the purposes of research, studies, training, voluntary service, pupil exchange schemes or educational projects and au pairing (hereinafter "Directive 2016/801/EU"). EU member states have until 23 May 2018 to enforce legal and administrative regulations necessary to achieve compliance with this Directive. The primary changes will concern particularly the provisions on long-term residence permits for study purposes and the definition of the term "studies". The main changes are summarised below.

- Introduction of long-term residence for the purposes of job seeking or initiation of business activity. This residence purpose will be intended for university students after the end of their studies in the country and for research workers who have completed their research activities. in these cases they will be allowed to remain in the territory of the Czech Republic for up to 9 months in order to look for employment or initiate business activity. However, this permit will not automatically mean the granting of the right to access the job market or to initiate business activity.

- Obligation to attend adaptation and integration courses. The efforts for the integration of foreigners residing in the territory of the Czech Republic in the long-term will no longer be on a voluntary basis only – the element of limited and corresponding obligation will be introduced: the conditions for residence in the country will include (in certain cases) the obligation to attend an introductory adaptation and integration course for new arrivals within one year of receiving their Czech residence permit.

The amendment introduces this obligation due to the identified necessity to inform foreigners especially about their rights and obligations as soon after their arrival in the Czech Republic as possible.

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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

Tax liabilities – June 2018

June

Monday, 11	Consumption tax	Tax maturity for April 2018 (except the consumption tax on alcohol)
Thursday, 14	Intrastat	The Intrastat statement for May 2018, paper version
Friday, 15	Income tax	Quarter or half-year tax advance payment
Monday, 18	Intrastat	The Intrastat statement for May 2018, electronic version
Wednesday, 20	Income tax	Monthly payment of deducted advance payments on personal income tax from employment
Tuesday, 26	Value added tax	Tax return and tax for May 2018
		EC Sales List for May 2018
		Tax control statement for for May 2018
	Energy taxes	Tax return and tax maturity on gas, solid fuels and electricity for May 2018
	Consumption tax	Tax maturity for April 2018 (only the consumption tax on alcohol)
		Tax return for May 2018
		Tax return for claiming of refund of consumption tax, for example on fuel oil, other petrol (benzine) for May 2018 (if applicable)

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Suspension of the OP PIK Subsidy Programme

An in-depth audit by the Ministry of Finance of the Czech Republic has highlighted errors in the Enterprise and innovation for competitiveness Operational Programme (hereinafter "OP PIK"), whose managing authority is the Ministry of Industry and Trade of the Czech Republic (hereinafter the "MoIT").

The situation has been reported by the MoIT to the national managing authority (the Ministry of Regional Development) and the European Commission, with which it is addressing the situation. Following the notice, the European Commission conducted an audit of the Operational Programme, identifying an exceptionally high – 14% – error rate in drawing subsidies, with the tolerated limit at a mere 5%. Therefore, the European Commission has decided to suspend the OP PIK certification, discontinuing the payment of funds for several months.

The suspension of OP PIK will not affect the payment of funds to approved projects in any way, with the funding covered by the MoIT using government resources for the time being. Subsidy recipients will continue to have the funds paid in the standard way to the applicant's account.
The suspension of the Operational Programme entails suspending the certification of funds from the EU budget to the state budget. As for open calls, the receipt of application is still underway, with new calls set to continue in line with the effective schedule. The MoIT has introduced internal measures aimed at reducing the error rate and is working with the European Commission to remove the errors. As a next step, the setup and conditions of individual subsidy programmes will be revised.

IT Firms at Threat of Not Receiving Subsidies

During the compliance audit of public support rules, it was noted that payroll costs of employees that had already worked at the firm could be reimbursed as part of the information and communications technologies projects under the ICT and shared services programme. However, according to the EU directives, support may only be provided to newly created jobs. Two already concluded calls are thus in breach of public support rules.

The MoIT has informed subsidy recipients in a dispatch that, under the current circumstances, their payment requests will be suspended. The subsidy recipients affected must state, by 31 May 2018, whether they will additionally create the jobs claimed or not. If existing employees had been transferred to newly created jobs as part of the project, it is necessary to replace their original positions. The MoIT has stipulated a period of three years within which the jobs must be created or replaced, which also applies to concluded projects. If the jobs claimed are created or replaced, the subsidy recipients will have amendments issued for the legal act, following the signature of which the reimbursement of payment requests will be renewed. If the subsidy recipient decides not to create or replace the new jobs, the payroll costs of employees not contributing to the net increase in the headcount of the given firm will not be considered eligible.

Given the matters outlined above, appendices to calls will be amended accordingly. New methodology is also being awaited, which should explain the above matters in greater detail. Given that it is a rather substantial change to the programme setup, the MoIT has also decided to set up a special e-mail and telephone line for subsidy recipients. The prevailing uncertainty, awaiting of a new methodology and changing rules may contribute to the growing lack of interest on the part of companies in drawing subsidies. This is on top of the fact that the Czech Republic is certainly not one of the countries having a keen interest in subsidy support.

A total of CZK 117 billion has been allocated for the Operational Programme for 2014-2020, yet only CZK 6.7 billion had been paid out as of 16 April 2018. Some firms want to defend themselves, refusing to bear the consequences of errors made by civil servants. Therefore, it is not ruled out that the state will be challenged in legal disputes.

Announcement of a National Call as part of the LIFE Programme

The Ministry of the Environment has announced a national call as part of the LIFE Programme for submitting applications for support in two sub-programmes – 'Environment' and 'Climate Action. Support may be applied for in the two sub-programmes not only for project co-funding, but also for preparing project documentation. Both public and private entities may apply for a subsidy, and the projects must be implemented in the territory of the Czech Republic, including the capital city of Prague.

Aims of the Call under the 'Environment' Sub-Programme:

- Environmental protection;
- Efficient and effective use of resources; and
- Environmental administration and information.

Support will be granted to projects focusing on the protection of nature and landscape, such as:

- Provision of safe and efficient use of water resources;
- Mitigation and compensation of land confiscation and better use of soil;
- Reduction in the amount of waste produced, maximisation of recycling; and
- Forest monitoring and information systems, and forest fire prevention systems.

Aims of the Call under the 'Climate' Sub-Programme:

- Climate change Mitigation;
- Climate change adaptation; and
- Climate-related administration and information.

Support will be granted to projects focusing on adapting to or mitigating climate change, such as:

- Transition to a low-carbon economy resistant to climate change;
- Sustainable farming and water and soil management; and
- Climate-related administration, including greater involvement of civil society, NGOs and local entities.

The subsidy per project is provided up to the amount of CZK 200,000 or CZK 240,000 for preparing project documentation, depending on the sub-programme, but no more than 15% of total eligible project costs. The maximum amount of eligible costs per project is CZK 10 million (net of VAT).

Receipt of applications for the 'Environment' Sub-Programme: 29 March – 3 May 2018.

Receipt of applications for the 'Climate' Sub-Programme: 29 March – 22 June 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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Remember to Publish Financial Statements

Publishing financial statements or the annual report ranks among an entity's regular duties. This article will summarise the essential requirements in this area.

Who is obliged to publish accounting information?

The methods of publishing accounting information are governed by Section 21a of the Accounting Act. The obligation to publish financial statements or the annual report rests only with reporting entities incorporated in the Public Register or to those in respect of which the obligation is stipulated by a special legal regulation. The obligation to publish financial statements or the annual report from 1 January 2016 also applies to Societies, Foundations, Institutions, Associations of Apartment Unit Owners and Public Service Organisations.

The Public Register is maintained by the Registry Court in an electronic form.

How is the information published?

The reporting entities incorporated in the Public Register publish relevant documents by filing them in the Collection of Deeds of the Public Register (the "Collection of Deeds"). The documents are to be sent to the relevant Registry Court in an electronic form in the PDF format. Each deed is filed as a single PDF document. One deed thus cannot be divided into several documents, nor is it possible to combine multiple deeds into a single PDF document. Documents may be sent to the Registry Court via a data box, e-mail, in the form of on-line filing, via a web application and on technical data media. More information is available here.

The Accounting Act provides an exemption for certain reporting entities that submit the annual report in the Collection of Deeds via the Czech National Bank.

What information is published?

Reporting entities are obliged to publish the following documents by submitting them to the Collection of Deeds:

- **Financial Statements** (ordinary, extraordinary and consolidated) or a summary statement of assets and liabilities (in the case of single-entry bookkeeping);
- **Annual Report** or a similar document if its preparation is required by the Accounting Act or a special legal regulation. Pursuant to Section 21 of the Accounting Act, the preparation of the annual report is required of the reporting entities the financial statements of which must be subject to audit.

In respect of financial statements for the period starting in 2016 or later:

- Reporting entities are **also obliged to publish a Report on Payments to Governments and** a consolidated report on payments to governments. The reports are prepared only by large reporting entities engaged in the mining and lumbering industries;
- **Small and micro reporting entities** that are not subject to mandatory audit may prepare a summarised version of financial statements and **do not need to publish the profit and loss account.** Therefore, they are only obliged to publish the balance sheet and the notes to the financial statements.

The financial statements may be filed as part of the annual report.

Pursuant to Section 66 (c) of the Registers Act, the Collection of Deeds also contains **Proposals for the Distribution of Profit** or the settlement of loss and their final wording (unless they form part of the financial statements).

Reporting entities are to publish the financial statements in the scope in which they prepared them. Reporting entities which are obliged to subject their financial statements to audit publish them in the scope and wording in which they were audited by the auditor.

When is the information to be published?

a. **The reporting entities which are obliged to subject their financial statements to audit** are to publish their financial statements and annual report:
   - After they have been audited by the auditor;
   - After they have been approved by the relevant body;
   - Within 30 days from meeting the two conditions stated above (unless special legal regulations stipulate otherwise);
   - No later than within 12 months from the balance sheet date of the financial statements to be published regardless of whether the financial statements were approved in the stated manner.

   The reporting entities are also obliged to publish the Auditor's Report and, if applicable, the information stating that the accounting records have not been approved. in addition, they must not publish previously unaudited information in a manner that might mislead the user into believing that it had been audited.

b. **The reporting entities which are not obliged to subject their financial statements to audit** are to publish their financial statements as well as annual report no later than within 12 months from the balance sheet date of the financial statements to be published. Given the unclear guidance in the amendment to the Accounting Act, certain lawyers believe that the obligation to publish the financial statements or annual report within 30 days from their approval by the relevant body also applies to the reporting entities that are not obliged to have their financial statements audited by independent auditors.

How is the selected information of the financial statements presented?

In the situation where the reporting entity only presents selected information from its financial statements, the reporting entity is to state that only selected details from the financial statements are disclosed and where the financial statements are kept. The auditor's report on the financial statements is not appended to the selected information; only the type of auditor's opinion on the financial statements and reference to any matters specifically emphasised by the auditor are disclosed.

What are the sanctions for breaching the obligations?

The sanctions for breaching the obligation to publish accounting information are stipulated by the Accounting Act as well as the Registers Act.

The Accounting Act from 1. 7. 2017 considers the violation of the obligation to duly submit the financial statements, annual report or report on payments to governments to the Collection of Deeds to be an **offence** on the part of the reporting entity.

The sanction pursuant to Section 37a is a fine of up to 3% of the total value of assets. in the first instance, the administrative offences of this sort are heard by the tax authority.

Pursuant to Section 72 (2) of the Registers Act, if the relevant document is not filed in the Collection of Deeds, the Registry Court will call on the incorporated entity to submit the document without unnecessary delay. If it fails to respond to the call, a disciplinary **penalty** of **up to CZK 100 thousand** may be imposed. However, if the incorporated entity repeatedly fails to meet its obligation to submit the required documents or if the failure to do so has serious consequences for third parties and if there is a legal interest in it, the Registry Court may, of its own motion, initiate the proceedings for the **dissolution of the incorporated entity including its liquidation** pursuant to Section 105 of the Registers Act. However, should this be the case, the Registers Court will notify the incorporated entity of this and will provide it with a reasonable deadline for remedying the deficiencies.

Furthermore, pursuant to Section 106 (2) of the Registers Act, the member of the statutory body of the legal entity which failed to meet its obligations pursuant to Section 105 of the Registers Act is in **breach of due managerial care**.

IASB has published a revised Conceptual Framework

On 29 March 2018, the International Accounting Standards Board (IASB) published its revised 'Conceptual Framework for Financial Reporting'.

The new Conceptual Framework does not constitute a substantial revision of the document as was originally intended when the project was first taken up in 2004. Instead the IASB focused on topics that were not yet covered or that showed obvious shortcomings that needed to be dealt with.

Included are revised definitions of an asset and a liability as well as new guidance on measurement and derecognition, presentation and disclosure.

The Conceptual Framework does not have a stated effective date and the Board will start using it immediately.

Together with the revised Conceptual Framework, the IASB has also issued Amendments to References to the Conceptual Framework in IFRS Standards. The document contains amendments to 14 standards and interpretations.

The amendments are effective for annual periods beginning on or after 1 January 2020.

We will bring more information about new Conceptual Framework in the next issue of our Accounting News.

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Amendments to IFRS 9 endorsed for use in the EU

On 22 March 2018, Amendments to IFRS 9 *Prepayment Features with Negative Compensation* 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 2019).

The Amendments to IFRS 9 were issued by the IASB in October 2017 to address the concerns about how IFRS 9 *Financial Instruments* classifies particular prepayable financial assets.

Changes

The amendments in *Prepayment Features with Negative Compensation* (Amendments to IFRS 9) are:

1. Changes regarding symmetric prepayment options

Under the current IFRS 9 requirements, the SPPI condition is not met if the lender has to make a settlement payment in the event of termination by the borrower (also referred to as early repayment gain).

Prepayment Features with Negative Compensation amends the existing requirements in IFRS 9 regarding termination rights in order to allow measurement at amortised cost (or, depending on the business model, at fair value through other comprehensive income) even in the case of negative compensation payments.
Under the amendments, the sign of the prepayment amount is not relevant, i. e. depending on the interest rate prevailing at the time of termination, a payment may also be made in favour of the contracting party effecting the early repayment. The calculation of this compensation payment must be the same for both the case of an early repayment penalty and the case of an early repayment gain.

2. Clarification regarding the modification of financial liabilities

The amendments also contain (in the Basis for Conclusions) a clarification regarding the accounting for a modification or exchange of a financial liability measured at amortised cost that does not result in the derecognition of the financial liability. The IASB clarifies that an entity recognises any adjustment to the amortised cost of the financial liability arising from a modification or exchange in profit or loss at the date of the modification or exchange. A retrospective change of the accounting treatment may therefore become necessary if in the past the effective interest rate was adjusted and not the amortised cost amount.

Effective date and transition requirements

The amendments are to be applied retrospectively for fiscal years beginning on or after 1 January 2019, i.e. one year after the first application of IFRS 9 in its current version. Early application is permitted so entities can apply the amendments together with IFRS 9 if they wish so. Additional transitional requirements and corresponding disclosure requirements must be observed when applying the amendments for the first time.

More information about Amendments to IFRS 9 can be found in our Accounting Newsletter from November 2017. The full version of the Amendments is available here.

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IFRIC 22 endorsed for use in the EU

On 28 February 2018, IFRIC 22 Foreign Currency *Transactions and Advance Consideration* was 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).

IFRIC 22 was issued by the IASB in December 2016 to clarify the accounting for transactions that include the receipt or payment of advance consideration in a foreign currency.

Scope of the interpretation

This Interpretation applies to a foreign currency transaction (or part of it) when an entity recognises a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration before the entity recognises the related asset, expense or income (or part of it).

Conclusions

- The date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration.
- If there are multiple payments or receipts in advance, the entity shall determine a date of the transaction for each payment or receipt of advance consideration.

Transition

On initial application, entities apply the interpretation either retrospectively or prospectively.

More information about IFRIC 22 can be found in our Accounting Newsletter from January 2017. The full version of the Interpretation is available here.

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ESMA publishes a report on the activities of accounting enforcers and their findings within the EU in 2017

On 3 April 2018, the European Securities and Markets Authority (ESMA) published a report on the enforcement and regulatory activities of accounting enforcers within the European Union in 2017.

ESMA is an independent EU authority that was established on 1 January 2011. ESMA's mission is to enhance the protection of investors and promote stable and well-functioning financial markets in the European Union (EU).

ESMA and the accounting enforcers in the EU are regularly examining compliance of financial information provided by listed issuers on regulated markets with the applicable financial reporting framework (IFRS).

In 2017, European enforcers examined the financial statements of about 1,100 issuers representing an average examination rate of 19% of all IFRS issuers with securities listed on regulated markets (2016: 21%). These examinations resulted in 328 actions taken to address material departures from IFRS (2016: 311). As in 2015 and 2016, the main deficiencies were identified in the areas of financial statements presentation, impairment of non-financial assets, and accounting for financial instruments.

In 2017, ESMA and European enforcers evaluated the level of compliance with IFRS in the areas identified as common enforcement priorities for 2016 annual IFRS financial statements on a sample of 204 IFRS financial statements examined by European enforcers. This assessment related to:

- Presentation of financial statements (IAS 1);
- Distinction between equity instruments and financial liabilities (IAS 32); and
- Transitional disclosures of the expected impact of IFRS 9 *Financial Instruments* in the financial statements of non-financial institutions.

Furthermore, ESMA, together with European enforcers, identified a set of common enforcement priorities highlighting topics significant for European issuers when preparing their 2017 IFRS financial statements. ESMA included:

- Disclosure of the expected impact of implementation of major new standards in the period of their initial application (IFRS 9, IFRS 15 and IFRS 16);
- Specific recognition, measurement and disclosure issues of IFRS 3; and
- Specific issues relating to IAS 7 such as reconciliation of liabilities arising from financing activities.

ESMA and European enforcers furthermore note that other issues such as the presentation of financial performance, the disclosures on the impact of Brexit and the disclosure of non-financial information and APMs will also be assessed.

ESMA also published a fact-finding exercise on disclosure of the impact of the new accounting standards (IFRS 9 and IFRS 15) in the 2016 annual and 2017 interim IFRS financial statements with the objective of assessing the level of transparency and effectiveness of disclosure on the impact of the implementation of the new standards.

ESMA Report on Enforcement and Regulatory Activities of Accounting Enforcers in 2017 is available on the ESMA website.

Source: www.esma.europa.eu

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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 24 April 2018.

As of 25 April 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 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)
- *Amendments to References to the Conceptual Framework in IFRS Standards* (issued in March 2018)

Interpretation

- IFRIC 23 *Uncertainty over Income Tax Treatments* (issued in June 2017)

Click here for the Endorsement Status Report

Invitation to Spring Seminar

IFRS 16 – New Standard on Leases

We would like to invite you to Deloitte's spring seminar on International Financial Reporting Standards, this time dedicated to new IFRS 16 *Leases*. IFRS 16 replaces IAS 17 *Leases* and the related interpretations and will be effective for the reporting periods starting on 1 January 2019.
The standard was endorsed for use in the EU in November 2017.

In the seminar, we will inform you about the key issues of this long-awaited standard, which predominantly introduces major changes in terms of lessees as operating leases will newly be recognised in the balance sheet. The application of the requirements arising from the standard will be illustrated in a number of practical examples. We will also provide answers to your inquiries in the seminar.

The seminar is predominantly intended for accountants, economists and financial managers of projects relating to IFRS and for all who want to know more about IFRS.

The seminar will be held in Prague in the Czech language and will be delivered by our professionals.

Date: Prague 16 May 2018

More information is available at: http://events.deloitte.cz/cs/

What Private Companies Should Know about the New Revenue Recognition Standard

If your company has not yet started addressing the application of the new US GAAP revenue standard, we would like to draw your attention to an interesting article published by Deloitte & Touche LLP on our website iasplus.com, which summarises the basic information on this new standard and specifically deals with differences and exceptions for private companies. The new revenue standard is effective for these companies for the annual reporting period beginning after 15 December 2018, as well as the interim period within annual reporting periods beginning after 15 December 2019.

The main points from the first part of the article are as follows:

- Private companies are required to adopt the Five-Step Model for Revenue Recognition
- The FASB gave private companies some relief related to disclosure requirements set out in the new revenue standard in the following areas:
  - Disaggregation of Revenue
  - Contract Balances
  - Performance Obligation
  - Remaining Performance Obligation
  - Significant Judgments
  - Contract Costs

The second part of the article is devoted to internal controls related to the adoption and application of the new Five-Step Model.

If you would like to find out more about this matter, we have additional publications on this area for you. You can also contact our experts who will be happy to meet with you to discuss this topic.

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Contacts

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The Joys and Sorrows of HR Specialists: How Will the GDPR Affect Databases with CVs and Other Employee Data?

Contact details, CVS, photographs and videos from corporate events only constitute a fragment of the data handled by HR specialists on a daily basis. HR departments process a large volume of personal data concerning both existing and previous employees as well as job applicants. However, the new General Data Protection Regulation (GDPR) requires setting new rules and verifying whether consents to personal data processing comply with the GDPR. If not, penalties may apply.

The practice indicates that consents are often useless or lack sufficient information (an employee did not receive appropriate information on personal data processing as required by the GDPR).

From May 2018, the General Data Protection Regulation will take effect. Companies and organisations thus have to prepare for new rules regarding personal data processing. What is the key? the legal basis of storing such data:

- **Statutory duties** – the duty to process personal data is stipulated by the Labour Code, other legal regulations as regards health, pension and sickness insurance etc.;
- **Performance of employment contracts (or agreements to work outside the scope of regular employment)**; and
- **Legitimate interest** – such as a CCVT system monitoring production (and thus also employees) because of personal protection.

The possibility of using the employee's consent to personal data processing, which has been often used by HR departments so far, will be limited to a great extent due to the new regulation. It will be possible to obtain the consent in situations in which another legal basis will not apply, ie in the absence of a specific legal duty or where the employment contract does not define any obligations in this respect etc. What situations does this particularly involve? For example, when the employer wishes to **publish photographs of its employees on the company's intranet**, it should have a consent from its employees to do so.

Step by Step: Employer's Duties

1. In the area of HR, employers should map all of their personal data processing procedures to determine which employee data are actually needed beyond the scope required by law or employment contracts.
2. For this purpose, it would be advisable to maintain **records on processing activities** specifying the name and contact information of the company, reason for data processing, description of the categories of data subjects and personal data, categories of data recipients, possible transfer of data to another organisation or country, deadline for such data erasure as well as a description of safety measures during processing.
3. It will be necessary to set an **internal personal data protection system** in line with the GDPR requirements.
4. Furthermore, the **existing consents** in the area of HR **will have to be reviewed** and revised according to the GDPR requirements; this especially involves completing the scope of and purpose for personal data processing.
5. If the employer intends to use new technology for data processing, or where the processing will pose a significant risk to employees, it will be necessary to assess the effect of **individual instances of processing** on personal data protection before the commencement of new processing, ie to assess and address the relating risks.

What is important? Do not forget that according to the GDPR, each consent should be **freely given, specific, informed and unambiguous**. Employees are rarely in a position towards their employers to give their consent freely, reject or withdraw it, which arises from the employer's superiority to employees.

Have you been overwhelmed by the GDPR? Are you at your wits' end? Why don't you try our GDPR Detective application resolving the mystery of personal data protection for you.

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The Constitutional Court's ruling on electronic sales records is the Act of the Year

The winner of the ninth annual Act of the Year survey is the initiative for more prudent regulation of business, i.e. The ruling of the Constitutional court on electronic sales records ("EET"). The expert public's votes ranked the Payment System Act implementing PSD2 second and the amendment to the Construction Act third. in this survey organised by Deloitte Legal, hundreds of entrepreneurs chose from five nominated legislative acts having a positive impact on business.

"*The results can be summarised as follows: Adopt new regulations with more consideration. and try to use new regulations to encourage innovation and improve the business environment, not stifle it*," says Tomáš Babáček, chairman of the nomination board of the Act of the Year survey and Deloitte Legal's attorney.

Complete results of the Act of the Year survey:

Rank	Topic	Result
1.	More prudent regulation of business (a Constitutional Court ruling on the electronic sales records)	37 %
2.	Regulation stimulating innovation on the financial market (the Payment System Act implementing PSD2)	25 %
3.	Legislative cut for fast-tracking construction (the Amended Construction Act)	18 %
4.	More efficient and effective court procedure (the Amended Code of Civil Procedure)	13 %
5.	Tax regulations reflecting business reality (the Amended Income Taxes Act)	8 %

The Act of the Year nomination board was composed of twenty authorities from various fields, not only business. This year's survey was held under the patronage of the Czech Chamber of Commerce and the Czech Bar Association. Voting was done using an online questionnaire and physical ballots at the individual partners of the project.

"*The fact remains that entrepreneurs themselves have an essential influence through the way they are able to self-regulate and sufficiently mobilise themselves when formulating requirements on the quality of new legislation*," summarises Tomáš Babáček from Deloitte Legal.

More information about the Act of the Year survey can be found at www.zakonroku.cz (Czech version only).

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