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TAX news

Grants & Incentives news

dReport: December 2018

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Current Situation as Regards the Tax Package Approval Procedure

The second reading of a bill amending various tax laws (the so-called Tax Package, Parliamentary Document No. 206) is to be included in the programme of the 24th session of the Chamber of Deputies, taking place from 4 December 2018.

As we have already informed you in previous issues and in our regular webcast, it is unlikely that the original bill will be passed by the year-end. The possible effect of changes specified in the original bill is being addressed at present. The motions to amend which have been considered and are available on the website of the Chamber of Deputies (the deadline for their submission was 14 November) do not clearly indicate a comprehensive approach. The Ministry of Finance is preparing and debating (for example with the Chamber of Tax Advisors of the Czech Republic) a proposal for postponing the effective dates of individual provisions, with the preliminary indication that selected changes would only come into effect after the Act has been passed (or from the next month following the publication in the Collection of Laws), with other ones becoming effective for the next taxation periods subsequent to the Act taking effect. We have been closely monitoring the latest developments. A summary of details concerning the Tax Package (including the effective dates of relevant provisions) will be published after the second reading.

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Possible Changes in the Real Estate Acquisition Act

The Czech Pirate Party has prepared a draft amendment to the ordinance on real estate acquisition tax which, if approved, would decrease the tax rate on the acquisition of real estate for natural persons purchasing real estate for own permanent residence and eliminate the possibility of claiming an exemption for new buildings by legal entities.

The first substantial change proposed by the deputies in the amendment to Ordinance of the Senate No. 340/2013 Coll., on Real Estate Acquisition Tax, relates to the exemption of the first transfer of a new building in exchange for consideration. At present, both natural persons and legal entities are entitled to the exemption, provided the property meets the statutory parameters of a new building. If the amendment is approved, the exemption could only be newly applied by acquirers that are natural persons, and EU and EEA nationals. According to the proposers, the amendment's objective is to prevent the existing practice whereby legal entities purchase new buildings and subsequently only sell equity interests in the given business corporations, which are not subject to real estate acquisition tax. The amendment should ensure that the legal entity pays real estate acquisition tax at least upon the first acquisition of the new building.

Secondly, the draft amendment proposes that the tax rate on real estate acquisition be decreased from 4% to 2% for tax bases under CZK 4 million. In excess of the limit, the standard 4% tax rate would continue to apply. The draft amendment proposes several conditions for applying this treatment: the decreased rate could only be applied by natural persons of age who are acquiring the whole property or an ownership interest equal to at least half of the property and who are not owners of another property in the Czech Republic or in another country as of the date of property acquisition, either directly or indirectly, for example, through a legal entity. The property must be intended for residence and, as of the date on which the deadline for filing the tax return expires, they must have permanent residence in the property. The latter condition is the weakest point of the draft amendment. In practice, if a natural person wanted to apply the decreased rate, he or she would have to relocate its permanent residence to the newly acquired property no later than within three months from the registration of the ownership right in the Land Register.

Another controversial restriction for applying the decreased rate is the five-year conditionality of the exemption: if the taxpayer gratuitously transfers his or her ownership

right to the property within five years from its acquisition, the entitlement to apply the decreased rate will expire and the taxpayer will be obliged to pay the remaining portion of the real estate acquisition tax at the standard 4% rate. Gratuitous transfers also include allocating the property to a trust fund. The restriction clearly targets the situations where the decreased rate would be abused for speculative purposes. However, neither the draft amendment nor its explanatory report specify the treatment of, for example, the settlement of marital property or divided co-ownership, which may occur on fully objective grounds.

At the moment, it is difficult to predict whether the amendment will find support in the legislative body. At its meeting of 24 October 2018, the government expressed a negative opinion. The draft is now set to be debated by the Chamber of Deputies. We will, of course, keep you informed about the course of the legislative proceedings.

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Ruling: Correction of Accounting Errors and Tax Base Implications

This article summarises the key information arising from judgment 3 Afs 28/2017 – 43 which was issued in October 2018, addressing two areas as follows: corrections in accounting records including implications for a corporate income tax return ("CITR") and insurance benefits in relation to an assigned receivable. A cassation complaint of the Appellate Financial Directorate ("AFD") against Československá obchodní banka (the "Company") has been rejected.

In 2008, the Company made corrections of its accounting records for a period of 2000-2005 (the aggregate amount of corrections of income and expenses was booked in 2008). These corrections were not reflected in the 2008 CITR; nevertheless, the Company filed additional CITRs for 2001-2004 (no additional CITRs were filed for 2000 and 2005 as these years were considered lapse periods). However, the Tax Office included the income in the 2008 tax base, without reflecting the related expenses in the tax base for the same year. According to the AFD, the Company failed to demonstrate that the expenses of the 2000-2005 taxable periods had not been booked in prior periods which is why the tax authority did not reflect those expenses in the 2008 CITR.

The Supreme Administrative Court ("SAC") ruled that the **tax authority cannot request the income/expenses to be reflected in the tax base for the taxable period in which the accounting correction was made** provided that the income or expenses relate to another taxable period. Furthermore, it is irrelevant that tax can no longer be additionally assessed for that taxable period because of a lapse of claim.

The judgment implies that if a retrospective correction was made in the accounting records due to an error, this would not affect the tax liability for the year in which the error was identified. We would like to note in this context that this involves corrections of errors made by mistake rather than deliberately to postpone the tax liability.

In addition, the Company provided a loan which was insured against risk at Exportní garanční a pojišťovací společnost ("EGAP"). An insured event occurred in 2003 (the receivable became uncollectible). Since that year, EGAP has paid out insurance benefits to the Company in an amount corresponding to the repayments of the original loan, as defined in the agreement concluded with the Company. Concurrently, the original receivable was gratuitously assigned by the Company to EGAP. In 2008, the Company recorded in its accounting records a receivable from EGAP, with the instalments recognised in the balance sheet as a decrease of the receivable's value. Nevertheless, from the tax authority's perspective, the Company concluded with EGAP an insurance rather than re-insurance contract for which reason Section 77 (a) (1) of Regulation 501/2002 Coll. does not apply and Section 27 of Regulation 500/2002 Coll. is used instead. As a consequence, insurance benefits should be recognised as income (not in the balance sheet).

It may be inferred from the SAC's ruling that differentiating between insurance and re-insurance is rather insignificant. The tax base cannot be determined solely based on accounting regulations. The **tax authority cannot additionally assess income tax based on the mere assertion that the accounting records of a company do not comply with its statements without concurrently providing convincing evidence of the true nature of the transaction** and, accordingly, its tax deductibility in the respective reporting period.

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GFD's New Guidance Note on the Binding Assessment of Transfer Pricing and the Method of Determining the Tax Base for Permanent Establishments

On 9 November 2018, a new guidance note, D - 32, of the General Financial Directorate ("GFD") was published in the Financial Bulletin of the Ministry of Finance on the binding assessment of the pricing method between related parties and the method of determining a tax non-resident's tax base on activities performed through a permanent establishment (hereinafter jointly as the "binding assessments").

The new guidance note replaces Guidance Note D – 333 and, besides changes relating to the binding assessment of pricing between related parties under Section 38nc of the Income Taxes Act, it also newly incorporates information on how to proceed during a binding assessment in assessing the determination of a tax non-resident's tax base on activities performed through a permanent establishment under Section 39nd of the Income Taxes Act, which was introduced as early as 1 January 2018, yet in respect of which no accompanying methodology has been issued so far.

Although the guidance note is not legally binding, it serves as a clue for tax payers as to how the tax administration will address the issue of transfer pricing between related parties and the determination of the tax base/tax loss in respect of permanent establishments.

Shortening the Deadline for Filing an Application

A major change introduced by Guidance Note D – 32 in respect of binding assessments is the clarification of the deadline for filing the binding assessment application. In line with the previously applicable guidance note, it was possible to file the binding assessment application both during the taxation period for which it was being filed as well as subsequent to its expiry until the deadline for filing the tax return for the period. The new guidance note clarifies the interpretation of the deadline for filing the binding assessment application in that, with effect from 1 January 2018, binding assessment applications may only be filed for the taxation period during which the application is filed and for the subsequent taxation periods.

The change may have a significant impact on applications filed subsequent to 1 January 2018 in compliance with the rules stipulated by the replaced Guidance Note D – 333. However, it still applies that in situations where the payer used the same transfer pricing method or method of attributing profits to a permanent establishment in the preceding periods under corresponding terms, it may be assumed that if an affirmative ruling is issued, the tax administrator will, despite the invalidity of the ruling for prior periods, proceed similarly during tax audits as if the binding assessment had been issued.

Who are the Applications to be Submitted to and who Issues the Binding Assessment Ruling?

The new guidance note also specifies that taxable entities must submit binding assessment applications to the locally competent tax administrator. The application will be examined either by the locally competent tax administrator or the General Financial Directorate depending on the number of domestic entities to which the binding assessment relates. If the application exclusively relates to payers falling within the competence of a single locally competent tax administrator, the ruling will be issued by the respective tax administrator. If the payers in respect of whom the ruling is issued fall within the local competence of multiple tax administrators, the application will be examined by the General Financial Directorate. The same procedure will apply to bilateral or multilateral advanced pricing agreements.

Uncertainty about the Issuing of Rulings Persists

However, the new guidance note fails to eliminate tax payers' uncertainty regarding the deadline for issuing binding assessment rulings as the tax administrator's deadline for binding assessments has not been clarified or determined in any way.

The Administrative Fee Depends on the Number of Transactions or Permanent Establishments

The administrative fee for accepting applications is not newly fixed at CZK 10,000 per application: its amount will depend either on the number of transactions or permanent establishments assessed.

Assessing a Set of Unrelated Transactions

In respect of the binding assessment of transfer pricing between related parties under Section 38nc of the Income Taxes Act, major changes include the approach to assessing a set of closely unrelated transactions with related parties. Pursuant to the previously applicable guidance note, if the tax administrator had issued a negative ruling, the rejection

of the application only related to the application itself, ie to all assessed transactions contained therein. Newly, the tax administrator will assess each transaction from among the set separately, independent of the others, with rulings issued on each transaction. These may be affirmative or negative regardless of the ruling on other transactions. The change in determining the administrative fee is also related to this update.

Assessing the Determination of the Tax Base in Respect of Permanent Establishments

With effect from 1 January 2018, Section 38nd of the Income Taxes Act also introduced a "binding assessment of the method of determining a tax non-resident's tax base on activities performed through a permanent establishment". Therefore, Guidance Note D – 32 specifies the methods for this type of binding assessment. In assessing the tax base for permanent establishments, the methods are similar to those in assessing transfer pricing. The primary basis are the tax non-resident's accounting books (tax records), with the tax base customary for tax residents in a similar situation taken into consideration. In determining the tax base, Section 23 (11) of the Income Taxes Act and Article 7 of the respective Double Taxation Treaty are applied, as are the general principles stipulated by the 2010 OECD Report on the Attribution of Profits to Permanent Establishments.

The assessment application must always be filed by the tax non-resident that has formed or will form a permanent establishment in the Czech Republic. If the tax non-resident generates profit in the Czech Republic through multiple permanent establishments whose activities are unrelated, each of them is separately assessed. However, if the activities of permanent establishments are inextricably linked, only one application may be filed and the permanent establishments will be jointly assessed. However, the administrative fee is again charged in a corresponding amount.

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The Court's New View on the Utilisation of Clinical Studies as Part of the R&D Deduction

The Supreme Administrative Court (the "SAC") has found against Vestra Clinics s.r.o. (the "Plaintiff") in the matter of the possibility of utilising clinical studies as deductible items for research and development ("R&D"). Although the Court confirmed that clinical studies do meet the definition of R&D (as is, after all, indicated in Guidance Note D-288 and the Frascati Manual), the SAC ruled that the Plaintiff's activities constitute the following of clearly defined instructions as prescribed by the clinical trial report, without containing any elements of novelty or clarifying scientific uncertainty.

The Court identified the elements with the clinical trial ordering party – the producer of the pharmaceutical – rather than with the Plaintiff. The SAC concludes that the Plaintiff merely carried out a specialised service for the ordering party: it did not bear the economic risk of the tested pharmaceuticals' failure or affect the instructions, course or conclusions of the clinical trials and thereby did not meet the conditions for utilising the R&D tax deduction.

The Plaintiff, as a non-governmental health-care facility (a CRO), performed Phase-3 clinical studies, ie the systematic testing of pharmaceuticals on patients with the aim of demonstrating and verifying their curative effects and identifying any undesirable effects. In doing so, the Plaintiff is not an entity developing the pharmaceuticals: the ordering party (a pharmaceutical company) only makes use of its technical facilities and the high level of expertise of its employees (physicians) in order to carry out this development phase.

Following an analysis of the Pharmaceuticals Act, the SAC concluded that clinical studies are, generally by their very nature, activities that may be subordinated under R&D as they comprise the two defining traits of R&D – the existence of an element of novelty and clarification of scientific uncertainty. However, the SAC added that for the activities to be utilisable as part of the R&D deduction, the negative condition stipulated by the Act must also be fulfilled: ie, that the activities carried out in implementing the project must be performed by the payer itself rather than purchased as a service.

What the Frascati Manual and the Horizon 2020 Programme Say

According to the SAC, the actual research activity was performed by the ordering party (the pharmaceutical company), with the ordering party having developed the pharmaceutical, including the instructions according to which the testing phase was carried out by the Plaintiff. Therefore, as the Court ruled, the Plaintiff did not carry the increased level of business risk – it was borne by the ordering party. If the result of the clinical trial had been negative, the development of the pharmaceutical would not have proceeded to the next phase: ie, the pharmaceutical

would not have been produced. According to the SAC, in this situation, the risk investment made by the clinical trial ordering party, rather than that of the Plaintiff, would have been marred.

The SAC thus refused to regard the clinical trial of a pharmaceutical performed by a CRO to constitute an independent R&D project whose input is a new active substance and the deliverable includes new findings on its actual effectiveness and safety. In its ruling, the SAC states that it regards clinical trials of pharmaceuticals to be eligible for a deduction only in relation to the development and subsequent commercial use of the pharmaceuticals as part of a single project. This is despite the fact that, globally, clinical studies are, as a rule, conducted by CROs (instead of pharmaceutical companies), which is also true of the Czech Republic.

Given this fact, it may be inferred that the authors of the Frascati Manual (the OECD's underlying document for identifying R&D activities) as well as, say, the authors of the documents for the Horizon 2020 programme – the principal EU programme supporting R&D activities (where the documents expressly state that Phase 1-3 clinical studies meet the definition of R&D) based the documents on the fact that clinical studies are, as a rule, carried out by CROs rather than pharmaceutical companies themselves. It may also be inferred that in preparing Guidance Note D-288, lawmakers based their work on the Frascati Manual and, as a result, made it possible for Phase 1-3 clinical studies to be utilised in a deduction as they meet the definition of R&D (which, after all, the SAC confirms).

Considering countries that have included the R&D deduction in one form or another in their legislation, you will find that the legislation of many of the countries (eg, France) makes it explicitly possible to utilise specialised activities and costs incurred on Phase 1-3 clinical studies as part of the deduction. In view of the matters outlined above, it is evident that the lawmakers or authors of the documents were interested in supporting the activities and were aware that not all phases preceding the roll-out of a new pharmaceutical are typically performed by a single entity. Subsequently, it is not relevant which entity implements this phase of clinical studies and whether it is implemented independently or as part of a greater whole (eg, along with the development of the pharmaceutical).

Who Carries the Business Risk?

In the case in hand, the result is a situation where, on the one hand, it has been confirmed that clinical studies constitute R&D, but, on the other hand, an argument is put forward referring to the use of "risk capital" during the product's development and its indivisibility from the whole being developed. However, it would be a mistake to assume that the Plaintiff did not carry the risk of a business failure. Its risk capital does not consist of the costs of bringing the development of the pharmaceutical into Phase 3, but, from its perspective, if it had selected inappropriate patients, carried out an erroneous analysis and made an incorrect expert assessment of the effects of the pharmaceutical administered by the physician, or selected and used inappropriate assessment methods, the investment would have been marred considering the costs incurred. At this point, it should be noted that while the Plaintiff's business risk does not consist of the failure to roll out the pharmaceutical, it would be at risk of losing a contractual partner and its professional reputation on the market if it made an error during the clinical research into the pharmaceutical's effectiveness and safety.

If the situation is misread, there is a risk of generalising the conclusions and applying them, say, to the automotive industry, whereby it could be asserted that if the payer only develops a certain component for a brand new engine, it does not bear the business risk of the failure of the entire item being developed (in this context, the engine). However, in business practice, it is entirely customary that multiple entities gradually participate in the development of a single whole, with by far not all of them bearing the business risk of achieving the target parameters. However, the situation described clearly shows how sophisticated the product or process being developed is. Distinguishing chains of development phases and assessing them from the business risk perspective could, in practice, result in the restriction of using the institutes of a deductible item by a whole series of firms performing undisputed R&D activities.

A Surprising Interpretation Given the Existing Legislation

In respect of the argument of acquiring the activities as a service, which is not, from the perspective of law, a tax deductible expense, it can also be objected that the interpretation is outside the boundaries of the existing legislation. By defining the impossibility of including a purchased service in R&D, the lawmakers had a completely different situation in mind: if the pharmaceutical company purchased the results of the Plaintiff's work, the purchase would not be tax-deductible on the pharmaceutical company's part. However, in this context, the Plaintiff did not purchase the service: it supplied it itself in the form of new expertly acquired findings which the ordering party ordered from it, as is customary in the industry.

Through this ruling, the SAC presented its view on the eligibility of R&D activities for a deduction, concluding that the Plaintiff lacked both the possibility of creatively affecting the instructions, course and assessment of the clinical trials, as well as the elements of novelty and business risk connected with testing a proprietary pharmaceutical.

The authors of this article believe that the ruling brings new insight into the definition of R&D activities eligible for a deduction which does not, however, decrease tax payers' legal uncertainty. With regard to utilisation, the results of Deloitte's latest survey indicate that uncertainty arising from ambiguous conditions of this aid constitutes the most significant barrier for almost 60% of businesses.

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Amendment to the VAT Act

As we have already informed you, the debate on the amendment to the VAT Act has been delayed and the relevant changes could become effective on 1 April 2019 at the earliest (instead of the originally anticipated date of 1 January 2019). In addition, a series of revisions have been submitted in relation to the amendment, which could further complicate the debate (these most frequently include proposed amendments to the application of VAT rates). At the same time, the signals that the existing VAT treatment should be preserved in respect of bonuses to statutory executives and members of statutory bodies have been ever greater.

Let us hope that as this dReport issue goes to press, the debate about revisions will have been concluded and the wording in which the amendment will enter the third reading in the Chamber of Deputies will be clear.

Reverse-Charge Extension

Starting from 1 January 2019, the VAT Directive was supposed to make it impossible for member states to apply selected reverse-charge treatments (eg, to trading in industrial crops or selected computer technology). However, the Council of the EU has adopted an amendment that also makes it possible to apply the reverse charge in the years to come (until the expected transition to the "Definitive VAT Regime").

Rulings of the CJEU

In Case C-502/17 C&D Foods Acquisition, the Court of Justice of the EU ("CJEU") ruled on how to treat the holding of equity interests in a subsidiary. The parent holding company did not provide any supplies to it (eg, in the form of management services), yet it provided such supplies to a "sub-subsidiary". The CJEU's ruling clearly shows that the holding of an equity interest in a subsidiary does not constitute an economic activity in terms of VAT regulations.

In Case C-495/17 Cartrans Spedition SRL, the CJEU described the treatment of export-related services. The CJEU did not depart from the direction implied in earlier judicature, yet it additionally clarified what evidence may be used to prove exemption. In our view, the ruling also substantially affects the interpretation of exemption pursuant to the Czech VAT Act.

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Hard versus soft Brexit. What will the divorce agreement with the EU bring?

The time of the withdrawal of Great Britain from the EU is inexorably approaching and the issue of Brexit has become a frequent topic of discussions. Although the political process regarding Britain's withdrawal from the EU has not come to an end yet, let's summarise the alternative scenarios and their possible impact.

Approval of the EU Divorce Agreement or "Soft Brexit"

In the past few days, the content of the agreement was finalised at last and approved by the British cabinet. However, it is still to be approved by the British Parliament and the result is far from being certain. The British Parliament should deal with the issue before Christmas. The agreement is also to be approved by the European Parliament.

The EU divorce agreement includes a transition period, which shall last until 31 December 2020, and which shall provide companies and individuals as well as state institutions with time to prepare for the final Brexit. The final relationship between the EU and Great Britain after the end of the transition period will be subject to a separate agreement.

During the transition period, Great Britain will continue to be a member of the customs union and the EU single market. Thus, no significant changes will occur for Britain from the perspective of customs and VAT, all the transactions will be Intra-Community transactions. During the transition period, Britain will not be able to apply its newly agreed deals or rules in areas governed by the EU.

Non-Approval of the Agreement with the EU or "Hard Brexit"

If the divorce agreement between Great Britain and the EU is not approved, Great Britain will leave the EU on the night from 29 March 2019 to 30 March 2019 under circumstances referred to as "hard Brexit". Under such scenario, Great Britain will be considered a third country with no custom concessions. All the imported and exported goods will be subject to standard customs procedures, including customs duty assessment. Further impacts are expected in the area of the origin of goods or matters related to the necessity to provide import/export licenses for certain groups of products.

In relation to VAT, it will be necessary to report the relevant transactions with goods as imports or exports. In the area of VAT, the existing procedures applied within the EU related to eg consignment supplies, triangulation, on-line sales of goods, using a single administration point or VAT refunds to persons from other EU member countries might also be affected in relation to Great Britain. Selected financial transactions with Great Britain will newly give rise to a VAT deduction claim.

Further Alternatives

The possibilities of postponing the deadline for Brexit or holding another referendum keep reappearing in the media. However, based on the statements of Theresa May, the British Prime Minister, such scenarios are not to be taken into account. Whether there is any justification for these alternatives will become clear only after the vote about the divorce agreement in the British Parliament.

Our Recommendations

With respect to the uncertain political situation in Britain, we recommend preparing for the possibility of a hard Brexit that does not provide any transition period. Only timely preparation for the possibility of a hard Brexit may eliminate the impacts that a hard withdrawal of Great Britain from the EU will bring.

We will be glad to provide you with a more detailed analysis or assist you in setting up efficient VAT and customs processes.

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A New Draft Act to Prevent the Double Taxation of Transactions with Taiwan

The Czech Republic has not concluded the standard international double tax treaty with Taiwan, as it has with the majority of other countries (as the Czech Republic does not acknowledge the territory of Taiwan as a state, it cannot conclude the contract).

In practice, this may have so far been to the detriment of Taiwan as a business partner as certain types of income generated by Czech firms and individuals coming from Taiwan had to be taxed in the Czech Republic regardless of whether the same transaction has already been taxed in Taiwan, and vice versa. As a result, several years of discussions have been held between the representatives of the two countries and, to prevent double taxation, the draft of a special act has been prepared, unilaterally introducing measures that typically form the content of international treaties. It is expected that Taiwan will introduce similar measures in respect of the Czech Republic.

The draft ensures the objective division of the right to collect income tax between the countries in situations where the source of the income is in one country and the recipient has residence in the other country. In practice, this includes, for example, income generated from construction, assembly and research activities, provision of technical advisory, use of patents, interest, equity investments etc. Furthermore, this also includes, for example, income from dependent activities, income of artists or athletes, and income from the use of copyright.

Based on the proposed legislation, double taxation will be eliminated in the Czech Republic through "**simple credit**".

In practice, this means that Czech residents generating income in Taiwan will have tax calculated in the Czech Republic from total income reduced by tax paid in Taiwan; however, the maximum amount that may be deducted must be proportional to the Taiwanese partial tax base. Exemption may be applied to personal income from dependent activities performed in Taiwan, with the income exempt from taxation in the Czech Republic if it has already been taxed in Taiwan.

The basic principles of eliminating double taxation are set to be as follows:

- Personal and corporate income will be primarily taxed in the country of the person's tax residence. It will only be taxed in the other jurisdiction under the conditions expressly defined by the provisions of the act.
- Profit from the business activities based in one jurisdiction directly performed in the other jurisdiction through a permanent establishment may be subject to taxation in the other jurisdiction, with the draft act also taking into account "**service permanent establishments**" (if the activities performed in the territory of the given jurisdiction exceed 9 months in any 12-month period).
- **Income from real estate** and its use or rental may be taxed in the jurisdiction where the assets are located.
- Profit from the sale of shares or other equity investments whose value is directly or indirectly derived from more than 50% of real estate located in the other territory will be taxed by the source country (the "**real estate clause**").
- In essence, it will be possible to tax **dividends, interest and licence fees** in both jurisdictions. If the recipient is a beneficial owner residing in the other country, the tax in the jurisdiction of the income's source must not, under the rules of the given territory, exceed the following thresholds:
  - Dividends – 10% of the gross amount of dividends.
  - Interest – 10% of the gross amount of interest. The rule does not apply to certain types of interest – eg, on loans for the acquisition of goods or equipment, and on loans guaranteed by governmental institutions (these are only taxed in the country of the interest recipient's residence).
  - Licence fees – 5% of the gross amount of licence fees for industrial, commercial or scientific equipment and 10% of the gross amount of other licence fees.

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Effect of a new Czech and Korean double tax treaty from January 2019

Overview

The new version of the double tax treaty between the Czech Republic and the Korean Republic is currently under discussion . The new double tax treaty shall replace the initial version of the treaty dating back to 1992 and substantially changes some areas. The new version provides a wider definition of a permanent establishment and changes the withholding tax rates on interest and dividends.

Service permanent establishment

The amended double tax treaty contains the definition of a service permanent establishment, which arises when services are performed on the territory of another contracting state for a period longer than nine months in any twelve-month period.

Taxation of passive income

Newly, the maximum tax rate of withholding tax on dividends shall be 5 percent for both legal and natural persons. According to existing rules, the dividends may be taxed at a 5 percent tax rate provided the recipient of the dividends holds at least a 25 percent capital share in the company distributing the dividends. The maximum tax rate of withholding tax on interest will be settled at 5 percent.

The withholding tax rate on royalties will stay unchanged, ie 10 percent. Zero percent withholding tax rate applies to any payments received as consideration for the use of, or the right to use, any copyright on literary, artistic or scientific work, including cinematograph films, films or tapes for television or radio broadcasting.

New rules for taxation of Capital Gains

A new paragraph (no. 4) of Article 13 Capital Gains introduces a provision for the taxation of gains derived by a resident of a contracting state from the alienation of shares or comparable interests. If more than 50 percent of their value is derived directly or indirectly from immovable property situated in the other contracting state, the gains may be taxed in that state.

Replacement of articles

Certain articles of the double tax treaty from 1992 were cancelled without replacement, ie Article 14 concerning the taxation of independent personal service or Article 21 concerning the taxation of the income of professors. The corresponding renumbering of articles was performed.

Additional option for elimination of double taxation

Another amendment concerns the elimination of double taxation. According to the new provisions, a Korean company shall be authorised to apply the offsetting method to the tax on dividends withheld by the Czech Republic. This benefit shall be available only if the recipient company holds a share of at least 25 percent in the share capital or voting rights.

New article in the treaty

A new Article 26 Entitlement to Benefits sets the rules for the revocation of benefits provided pursuant to the provisions of the double tax treaty if the relevant transaction was performed without any economic substance and with the only objective to obtain benefits.

Summary

The amended version of the Czech and Korean double tax treaty was concluded on 12 January 2018. The Senate of Parliament of the Czech Republic approved the ratification of the treaty on 17 October 2018. The negotiation about the treaty is on the schedule of the Chamber of Deputies of Parliament of the Czech Republic starting on 4 December 2018.

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News round up

Belgium: cooperative tax compliance program

The Belgian tax authorities are launching a pilot cooperative tax compliance program (CTCP) for "very large enterprises", intended to establish "further collaboration between the tax authorities and the enterprises, based on trust, transparency and faster legal certainty, in order to enhance compliance". Participation in the CTCP will be available only to very large enterprises and must include all members of the group (i.e. resident or non-resident companies and permanent establishments in Belgium, based on consolidation rules). A participating company also will need to comply with a number of other conditions, including timely filing of tax returns; no outstanding tax liabilities; and no significant late payment interest charges, or instances of negligence, violations or fraud in the last three years. The company also must have a functioning tax control framework. The CTCP will cover income tax and taxes associated with income tax, VAT and other miscellaneous taxes as listed in the Belgian tax authorities' announcement. There is no opt-out and the CTCP will always cover all of these taxes.

Germany: draft of Brexit Tax Implementation Act

On 9 October 2018, Germany's Ministry of Finance (MOF) issued a draft law that would introduce tax measures to protect German taxpayers from potential negative consequences of the UK leaving the EU (Brexit Tax Implementation Act). After the UK leaves the EU without a transition period or a withdrawal agreement ("hard Brexit"), the UK will be treated as a country outside of the EU and will no longer be able to benefit from certain German tax measures that are available only to EU-resident taxpayers. To mitigate the most disadvantageous tax consequences resulting from Brexit, the draft law clarifies that Brexit itself will not constitute a "harmful event" for purposes of certain German tax law provisions. If approved, the draft law would become effective on 29 March 2019.

Jersey: new economic substance requirements

On 23 October 2018, Jersey's Minister for External Relations presented draft legislation that would introduce increased substance requirements on certain Jersey resident companies. If approved, the measures would apply as from 1 January 2019 and affect Jersey resident companies with accounting periods commencing on or after that date that undertake "relevant activities." Nine relevant activities would fall within the scope of the proposed rules. These are: banking, financing and leasing, intellectual property holding, fund management, shipping, headquarter activities, insurance and holding company activities and distribution and service centre business.

Netherlands: consultation of implementation of ATAD II

The Dutch government launched a public consultation on 29 October 2018 on potential changes to the corporate income tax act to implement various provisions of the EU Anti-Tax Avoidance Directive (ATAD II), targeting hybrid mismatches in EU and third-country situations. The consultation period will last until 10 December. The ATAD II aims to prevent a (deemed) deduction without inclusion or (deemed) double deduction situations resulting from a hybrid mismatch. The proposed Dutch rules would mainly apply between related parties, basically requiring an ownership interest of at least 25%. A hybrid mismatch may involve a hybrid entity, a hybrid instrument, a hybrid permanent establishment (PE) or a dual resident entity. In addition, a specific provision is proposed for imported hybrid mismatches.

Netherlands: confirmation of CJEU decision in fiscal unity cases by Supreme Court

The Dutch Supreme Court issued a decision on 19 October 2018 confirming the February 2018 decision of the Court of Justice of the European Union (CJEU) on the compatibility of the Dutch fiscal unity regime with EU law. The case had been returned to the Dutch court for a final decision. On 22 February 2018, the CJEU ruled on two joined cases referred by the Dutch Supreme Court. One case involved the anti-profit shifting rules and the other the deduction of currency losses. The CJEU held that the Netherlands cannot apply rules (e.g. anti-profit shifting rules) that generally are applied in both domestic and cross-border situations, but whose effect is more advantageous by entering into a fiscal unity. Since a fiscal unity is available only to Dutch resident companies, the more advantageous treatment is limited to domestic situations. The CJEU concluded that the Netherlands may not deny certain benefits ("elements") of the fiscal unity regime in EU situations simply because EU-resident companies are not allowed to be included in a fiscal unity and, therefore, the anti-profit shifting rules are incompatible with the freedom of establishment principle in the Treaty on the Functioning of the European Union. The CJEU held that the rules relating to currency losses are compatible with EU law. The Supreme Court has now confirmed the CJEU decision, putting an end to the debate on the per element approach.

Spain: draft bill for tax measures

On 23 October 2018, the Spanish government released three draft bills to implement some of the tax measures proposed in the 2019 budget. The bills would introduce new taxes on digital services and financial transactions, as well as measures

to amend the domestic exit tax and controlled foreign company (CFC) rules to transpose the EU Anti-Tax Avoidance Directive (ATAD 1) into domestic law. The bills on the tax on digital services and the tax on financial transactions would enter into force once a three-month period has elapsed from the date the relevant law approved by parliament is published in Spain's official gazette. The measures transposing ATAD 1 are expected to apply to fiscal years starting on or after 1 January 2019.

UK: taxation of digital services

Key measures impacting non-UK owned groups announced in the 29 October 2018 budget include the introduction of a 2% digital services tax as from April 2020, applicable to groups with global revenue from such activities exceeding £500 million a year and income generated in the UK exceeding £25 million. The rules will include safe harbour provisions that reduce the effective rate of tax on businesses with very low profit margins. DST also will be an allowable expense for UK corporate tax purposes and it will not be creditable against corporation tax. The Chancellor made clear that the government would prefer a global tax framework on this matter, but in the interim, this measure will be introduced unilaterally. DST, therefore, is badged as a temporary measure and will cease to apply once a comprehensive global solution is in place.

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Tax liabilities – December 2018

December		
Monday, 10	Consumption tax	Tax maturity for October 2018 (except the consumption tax on alcohol)
Friday, 14	Intrastat	Submission of statements for intrastat for November 2018, paper form
Monday, 17	Road tax	Advance payment on tax for October and November 2018, possibly the maturity of one advance payment of tax (minimally in amount of 70 % of the annual tax obligation) - in a case of taxpayer, who is an operator of trucks, trailers and semitrailers with maximum allowed weight of 12 tonnes and more, to whom the tax is decreased by 48 % according to § 6 paragraph 10 based on Act on Road Tax
	Income tax	Quarter or half-year tax advance payment
Tuesday, 18	Intrastat	Submission of statements for intrastat for November 2018, electronic form
Thursday, 20	Income tax	Monthly payment of deducted advance payments on personal income tax from employment
Thursday, 27	Value added tax	Tax return and tax for November 2018
		EC Sales List for November 2018
		VAT control statement for November 2018
	Energy taxes	Tax return and tax maturity on gas, solid fuels and electricity for November 2018
	Consumption tax	Tax maturity for October 2018 (only the consumption tax on alcohol)
		Tax return for November 2018
		Tax return for claiming of refund of consumption tax, for example on fuel oil, other petrol (benzine) for November 2018 (if applicable)
Monday, 31	Income tax	Payment of special-rate withholding tax for November 2018

Tax liabilities – January 2019

January

Wednesday, 9	Excise tax	Tax maturity for November 2018 (excluding excise tax on alcohol)
Monday, 21	Value added tax	Tax return and tax maturity to MOSS
	Income tax	Monthly deduction of the sum of deducted advance payments for personal income tax from dependent activity
Thursday, 24	Excise tax	Tax maturity for November 2018 (only excise tax on alcohol)
Friday, 25	Gambling tax	Tax return and tax maturity for 4th quarter of 2018
	Value added tax	Tax return and tax for 4th quarter and for December 2018
		Summary report for 4th quarter and for December 2018
		Control report for 4th quarter and for December 2018
	Energy taxes	Tax return and tax maturity on gas, solid fuels and electricity for December 2018
	Excise tax	Tax return for December 2018
	Excise tax	Tax return for claiming of refund of consumption tax for example on fuel oil and other petrol (benzine) for December 2018 (if applicable)
Thursday, 31	Biofuels	Reporting according to Section 19 (8) Act no. 201/2012 Coll.
	Road tax	Tax return and tax for 2018
	Real-estate tax	Tax return (completely) or partial tax return for 2019
	Income tax	Withholding tax payment based on special tax rate for December 2018

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Latest Schedule of OP PIK Calls

The table below presents the latest schedule of the calls already announced under the Enterprise and Innovation for Competitiveness Operational Programme ("OP PIK"), including the deadlines for submitting applications for aid in individual programmes.

Programme name	Programme focus	Type of call	Subsidised territory	Types of recipients*	Planned deadline for submitting aid applications
'Potential' Call V	Subsidy for establishing or developing industrial research, development and innovations centres	Round-based	Czech Republic excluding the capital city of Prague	SME, LE linked to the environment or in cooperation with an SME	From 1 Oct 2018 To 3 Jan 2019
'Applications' Call VI (both with or without effective cooperation)	Subsidy for implementing industrial research and experimental development	Round-based	Czech Republic excluding the capital city of Prague	SME, LE linked to the environment or in cooperation with an SME	From 28 Aug 2018 To 17 Dec 2018
'Real Estate' Call III	Subsidy for modernising production operations and renovating the existing outdated business infrastructure and brownfield sites	Ongoing	Czech Republic excluding the capital city of Prague	SME	From 22 Oct 2018 To 22 May 2019
'Energy Savings in Heat Distribution Systems' Call III	Subsidy for renovating and developing head distribution systems, and increasing the efficiency of cogeneration	Ongoing	Czech Republic excluding the capital city of Prague	SME, LE	From 11 June 2018 To 31 Mar 2019
'Energy Savings' Call IV	Subsidy for activities relating to final energy consumption savings	Ongoing	Czech Republic excluding the capital city of Prague	SME, LE	From 2 July 2018 To 29 Apr 2019
'Renewable Energy Sources' Call IV	Subsidy for projects relating to generation and distribution of renewable energy	Ongoing	Czech Republic excluding the capital city of Prague	SME, LE	From 3 Aug 2018 To 29 Mar 2019
'ICT and Shared Services – Formation and Operation of Shared Service Centres' Call IV	Subsidy for forming and operating shared service centres	Ongoing	Czech Republic excluding the capital city of Prague	SME, LE	From 28 Aug 2018 To 28 May 2019
'ICT and Shared Services – Development and Modernisation of Data Centres' Call IV	Subsidy for modernising and developing data centres	Ongoing	Czech Republic excluding the capital city of Prague	SME, LE	From 31 Aug 2018 To 31 May 2019

** SME – small and medium-sized enterprises, LE – large enterprises*

In early November, the schedule of OP PIK calls was updated, with the 'ICT and Shared Services – New IS/ICT Solutions Design' Call moved to calls to be announced. Based on the latest schedule, four calls are planned to be announced in December:

- 'Innovative Vouchers' Call IV
- 'MARKETING – IVV' Call IV
- 'Technology – Industry 4.0' Call IX
- 'Proof of Concept' Call II

2020: a Crucial Year in Subsidies

The current programming period of the Enterprise and Innovation for Competitiveness Operational Programme ("OP PIK") has been stipulated for the period from 2014 to 2020. Therefore, 2020 will be a landmark year.

A series of as yet successful calls are planned to be announced prior to the end of the programming period.

In early 2019, it will be possible to submit applications for aid under the 'Technologies for Emerging Entrepreneurs' and 'Technologies – Industry 4.0' calls. It will be possible to submit applications for the two calls until May 2019.

Approximately in mid-2019, the 'Innovation' (May 2019) and 'Application' (July 2019) calls are planned to be opened. The calls are additionally planned to be announced in Q1/2020. As part of the planned 'Innovation' calls, projects focusing on the issue of drought are considered to be favoured.

A series of measures are planned to be adopted before the end of the current 2014–2020 programming period. These primarily include the new activity "Acquisition of Digital Technical Maps and Formation of a Coal Platform". It will cover the coal-mining regions – the Moravian-Silesian, Ústí nad Labem and Karlovy Vary Regions – which will be able to receive a greater portion of funds through subsidies.

The upcoming 2021–2027 programming period will primarily support activities relating to low-carbon economy, industrial energy savings and renewable sources of energy, Industry 4.0, digital and smart economy, and effective use of resources as part of circular economy. Financial tools such as loans, guarantees, equity investments and others will constitute a significant feature of aid in the new, post-2021 programming period.

European Commission Approves an Investment Package of EUR 243 Million from the EU's Budget for LIFE Projects

On Thursday, 25 October, the European Commission approved an investment package of EUR 243 million from the EU's budget to fund projects under the LIFE Programme.

The programme supports projects focusing on the conservation of nature and the landscape, the environment, and climate across the whole European Union. The project's objective is to promote the development of low-emission economy and contribute to the conservation of the environment and biodiversity. The programme started in 1992 and has since supported over 4,600 projects in the European Union and third countries.

Of the total EUR 243 million, EUR 196.2 million will be allocated to supporting projects related to the environment and efficient use of resources, nature and biodiversity, environmental management and raising awareness of the environment. The remaining EUR 46.8 million is earmarked for projects focusing on the mitigation of climate change, adaptation to it or climate management.

Based on the sub-programme, corporate entities, public entities, universities, scientific research institutions and others will be eligible to apply for aid.

Planned Announcement of Call No. 97 under the 'Employment' Operational Programme

The call is set to be announced by the Ministry of Labour and Social Affairs of the Czech Republic. Call No. 97 is included in the "Support of Employment and Workforce Adaptability" priority axis, which focuses on supporting employee professional training with emphasis on technical and key competencies that may relate to IT, languages, soft skills or technical skills.

Employee training is eligible for aid of CZK 500,000 – CZK 10,000,000. Newly-formed firms may apply for a maximal amount of CZK 2,000,000.

The call is planned to be announced in March 2019, with the deadline for submitting applications for aid set to expire in May 2019.

Changes to OP PIK Project Administration

The Ministry of Industry and Trade has issued a new document – Categorisation of Types of Changes to Projects – which came into force on 30 October 2019. The newly promulgated document informs subsidy applicants and recipients about individual types of changes to projects and about which of them are permitted and which are not. Furthermore, the document provides information about the necessary change-related administration and deadlines for making changes or, to be precise, filing an application for a change.

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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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