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New mandatory annex to the corporate income tax return concerning related parties

The Czech Tax Administration is preparing a new annex to be electronically attached by selected entities to the corporate income tax return for the first time for the year 2014.

The aim of the annex is the collection of basic data on selected transactions conducted with related parties, such as statements of where the related party has its registered office, transaction volume, lists of mutual claims and liabilities, etc. Transactions shall be shown by type – e.g. sale of goods, provision of services, licence fees, interest, fixed assets, etc. The annexes are to be submitted separately for each related party; however, details on the volume of mutual transactions are to be filled in only if the taxpayer's mutual transactions with related parties have exceeded CZK 10 million in a given calendar year.

Companies that have met at least one of three criteria for mandatory audit, i.e. assets exceeding the sum of CZK 40 million or net turnover exceeding CZK 80 million or an average number of (full-time equivalent) employees exceeding 50, should fill in this annex. If the company shows a loss or was promised investment incentives, it should fill in the annex for all those related parties with which it conducted a transaction in the given period. In all other cases, it should state only those transactions with related parties based abroad, if any.

It can be advantageous for selected entities obliged to fill in this annex to so set up their accounting system in advance as to be able to record transactions separately for each related party.

We can expect that the tax administration will use the information collected to more efficiently analyse and identify companies for future tax inspections focusing upon transfer pricing between related parties. This is another indication of the Czech tax administration's recent increased focus on transfer pricing.

Taxpayers falling under the competence of the Specialized Tax Office (companies whose turnover exceeds 2 billion CZK, banks, insurance companies and other financial institutions) have received a questionnaire containing similar requirements to the new annex to the tax return. However, the questionnaire is to be filled in retroactively for the year 2013.

We will be glad to assist you with filling in the questionnaire for the year 2013 as well as the new annex for the year 2014: please feel free to contact us.

Abolition of tax deduction for pensioners was unconstitutional

On 30 July 2014 the Constitutional Court ruled that the existing regulation of the basic tax credit in the case of working old-age pensioners was unconstitutional.

In 2012 the amendment to Act no. 586/1992 Sb., the Income Tax Act, as amended, was adopted, on the basis of which the basic taxpayer's tax credit amounting to CZK 24 840 could not be claimed if on 1 January of the given tax year the taxpayer was in receipt of a retirement pension from the pension insurance scheme or from a foreign compulsory insurance of the same type.

The above-mentioned provision has been considered problematic from the beginning and triggered resentment among taxpayers. As a consequence, many old-age pensioners “de-registered” from the retirement pension scheme on 1 January 2013, only to restart receiving the retirement pension on 2 January 2013 so that they were not in receipt of a retirement pension on 1 January 2013 and thus could claim tax credit. As a rule, the tax administration did not consider such an approach legitimate and warned that it might qualify as a circumvention of the law or an abuse of rights



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The Constitutional Court found the above legislation to be unconstitutional due to inequities between particular groups of taxpayers. The Court pointed out that at the lower retirement pension the individual pensioners received a heavier tax burden and this inequity is precisely where the Constitutional Court sees a flaw. At the same time, the Constitutional Court found no reasonable cause to set 1 January of the given year

as the decisive day for tax credit entitlement, disproportionately favouring old-age pensioners who were awarded retirement pensions in the course of the year.

Thus the Constitutional Court abolished the above legislation with effect from the day on which the finding was published in the Collection of Laws, i.e. 4 August 2014. As a result, all taxpayers are entitled to tax credit for the tax year 2014 amounting to CZK 24 840, including those who on 1 January 2014 were in receipt of a retirement pension from the retirement pension scheme or a foreign compulsory insurance of the same type.

According to the tax administration, age old pensioners can claim tax credit for the first time within the monthly payroll processing for August 2014. The basic requirement is that the taxpayer carries out the respective changes in the declaration of a taxpayer liable to personal income tax from dependent activity. Employees do not lose tax credit for January to July 2014. Within the annual tax settlement which the employer carries out at the employee's request (by 31 March 2015), the employer includes the basic tax credit and returns the overpaid tax to the employee. If an employee has not claimed this tax credit in the course of 2014, he or she can claim it subsequently in the application for an annual settlement of income tax advance payments for 2014. Similarly, the employee can include it in his or her tax return.

Old age pensioners who submit their personal income tax return for the year 2014 should claim tax credit in full in the amount of CZK 24 840.

The Constitutional Court's finding applies only to 2014 and subsequent years. The tax liability of old-age pensioners for 2013 shall therefore remain unaffected: there is no option to claim tax credit for 2013 retroactively.

Payment of tax for employees hired from an employment agency non-resident in the Czech Republic

Companies in the Czech Republic often make use of employment agencies' services. Many of those agencies do not have their registered office in the Czech Republic but only a branch without legal personality.

Under the present legislation, if a Czech company hires an employee from an employment agency which has no registered office but only a branch in the Czech Republic, the Czech company is obliged to pay personal income tax from dependent activity. If, however, the company hires employees from an employment agency resident in the Czech Republic, the agency is liable to pay tax.

In this context, the Court of Justice of the European Union and subsequently the Czech Supreme Administrative Court issued judgements stating that the Czech Income Tax Act is in conflict with European law as regards the rule regarding who is liable to pay tax for employees hired from an employment agency with its registered office outside the Czech Republic.

Both courts have consistently stated that European law precludes such legislation according to which companies with their registered office in one Member State that make use of employees employed and temporarily assigned by employment agencies that have their registered office in another Member State but that carry out their activity through a branch in the first Member State are obliged to deduct tax advances from the income of the stated employees, whereas companies with their registered office in the first Member State that make use of services of an employment agency resident in the same State have no such obligation.



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In other words, it is not possible to require a Czech company which hires workers from an employment agency with a mere branch but no registered office in the Czech Republic to pay tax for the assigned employees.

The Czech tax administration has not issued a public opinion on this issue. Neither does the prepared amendment to the Income Tax Act include a corresponding change in the relevant provisions. We will keep you informed of developments.

If you need any additional information, please feel free to contact us.

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