

Tax Flash

Tax Flash is an electronic newsletter prepared by PricewaterhouseCoopers Česká republika, s.r.o. to keep you up to date on the latest tax and legal news. A more complex look at key tax changes and their impact on your business is provided in our monthly newsletter, Tax & Business News.

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Czech Republic

18 July 2014

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Czech Republic: Mandatory reporting of related-party transactions

The Czech Tax Administration has recently announced a new reporting obligation for legal entities which participate in transactions with related parties. The taxpayers will be obliged to file a separate disclosure form – “Overview of Transactions with Related Parties” – together with the corporate income tax return (“CITR”). This disclosure form shall be required for the taxable period 2014 and later periods.

The disclosure reporting of related-party transactions will be required for those legal entities that meet at least one of the following conditions for the statutory audit in the respective taxable period:

- Total assets exceeding the amount of CZK 40 million (approx. EUR 1.5 million);
- Net turnover exceeding the amount of CZK 80 million (approx. EUR 3 million) per annum;
- Average number of employees exceeding 50.

Furthermore, the taxpayer should participate in at least one transaction with its related party while at the same time:

- Related party has its registered seat outside the Czech Republic; or
- Taxpayer reported a loss in the respective taxable period; or
- Taxpayer is a recipient of investment incentives.

A separate disclosure form will need to be prepared for each related party, notwithstanding the number or materiality of transactions with that particular related party. The disclosure form includes basic information about the related party, its name and place of residence (i.e. country) and includes the following information regarding the volume of transactions with the related party:

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| • Purchase/sale of long-term assets; | • Received services; |
| • Purchase/sale of stocks, materials; | • Interests and royalties; and/or |
| • Sale of products, goods and services; | • Receivables and payables with related parties. |

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The disclosure reporting of related-party transactions will be used by the Czech tax administration in a risk analysis when selecting entities for a tax audit. The specific issues that are the focus of the tax administration include:

- The assessment of transaction's significance;
- The market situation;
- Usage of tax haven;
- Appropriateness of management fees, licence fees and interest rates;
- Business restructuring; and/or
- Long-term losses.

We expect that the number of audits in the area of transfer pricing from the Czech tax administration will increase in the coming years, and that audits will be more focused on "high risk" areas and specific transactions selected through the disclosure reporting. In addition, the Czech tax administration is planning to send voluntary questionnaires to selected Czech corporate taxpayers to obtain further financial information on transfer prices and payments with related parties.

We can provide assistance to clients to help them prepare for this reporting obligation, and advise them on what risks can follow from information provided to tax authorities within the reporting and how to mitigate such risks. Our services include:

1. Preparation of the disclosure form

We will assist with the preparation of the disclosure form (i.e., a separate form for each related party). The company will have the benefit of the streamlined process and low cost to prepare the disclosure form.

2. Basic risk assessment of related-party transactions

We will evaluate potential risks related to a company's related-party transactions based on the information included in the disclosure form and provide advice on how to mitigate these risks.

The company will know the potential outcome of the risk assessment review that will be performed by the tax administration and will be better prepared for a potential tax audit.

3. Detailed analysis of related-party transactions

We will perform a detailed analysis of the related-party transactions including their nature, price methodology and available supporting documentation, and examine the arm's length nature of the transactions. We will propose further steps in order to mitigate related risks.

The company will be well prepared for a potential audit investigation and will be able to make proactive modifications to the pricing policy and/or prepare the documentation and consider broader changes and opportunities for the business and pricing model.

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4. Transfer pricing documentation

We will prepare transfer pricing documentation supporting the arm's length nature of the transactions.

The transfer pricing documentation will serve as a tool to defend prices during a potential tax audit and will follow the specific local requirements and guidance of the tax administration.

5. Advance Pricing Agreement ("APA")

We will prepare an application for a binding ruling from the Czech tax administration on the methodology used in the pricing of specific transaction(s) with related parties and support the company in its negotiations with the tax administration.

The APA will provide certainty over the transfer prices for the period of three years from the Czech (unilateral), or Czech and foreign (bilateral/multilateral), perspective.

The takeaway

The new disclosure reporting for related-party transactions in the Czech Republic is expected to serve as a risk-assessment tool of the tax administration to identify taxpayers (and specific transactions) for a tax audit. The disclosure form is not intended to replace the transfer pricing documentation, preparation of which is not obligatory in the Czech Republic, but it is highly recommended and is typically requested during a tax audit..

For a discussion of how this new rule might affect your business, please contact our **transfer pricing** experts:



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