

# Tax & Business News

Tax, accounting, advisory and assurance newsletter

July|2009

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Dear Business Partners,

Welcome to the July edition of Tax & Business News in which we bring you updates and news from the area of tax, accounting and financial advisory.

In this month's Tax & Business News we cover a wide range of issues, including parliamentary changes concerning the administration and payment of taxes, electronic filings for customs declaration and excise declarations, new rules for IFRS reporting, an amendment to the Act on Protection of Economic Competition, recent trends in the pharmaceutical industry, and current conditions in the Czech Job market. However, the article that strikes me as the most significant is the one covering the RLRE Tellmer Property European Court of Justice (ECJ) case. Why is this? Well it isn't because of the subject matter to which the judgment relates, interesting through it is. The reason, in my view, for the significance of this particular article is that it reports the first VAT case ever to be referred to the ECJ by the Czech courts, despite the fact that the Czech Republic has been a member of European Union (and subject, therefore, to a VAT system based on the European VAT Directive) for more than five years now. So why has it taken so long for a VAT case to be

referred to Europe? Is it because Czech VAT payers don't have contentious issues worthy of litigation? The sheer mass of VAT cases referred to the ECJ by other EU Member States over the last three decades would suggest that this is not the case. The answer, I suspect, may therefore simply be that, until now, the Czech courts just haven't been in the habit of referring VAT issues to the ECJ and that those who have been supporting VAT payers litigating against the Tax Authorities haven't put strong enough arguments forward for their doing so. If there is enough at stake, and a VAT payer (or his advisor) can persuade the courts that there is sufficient doubt in a case for a question to be referred to the ECJ this, in the context of VAT disputes, should be a natural next step, not a last resort. Let's hope that for the sake of all Czech Businesses who have a VAT dispute where they believe a referral to the ECJ is appropriate, the RLRE Tellmer Property case is the sign of things to come.

Yours sincerely,  
Peter Skelhorn  
Partner, Tax and Legal Services

## Four pieces of tax news from Parliament

During its third reading, the Parliament approved amendments to the Income Taxes Act, the Administration of Taxes Act, and the new Tax Administration Code. The most important news of the new legislation is the following:

### Income Taxes Act: Lump sum for operating motor vehicles

- For the taxable period starting in 2009, an alternative to claiming actual costs related to operating motor vehicles – the possibility of claiming costs as the lump sum amount of CZK 5 000 – has been approved. On top of this lump sum, it is still possible to claim tax depreciation as a tax-deductible expense, on the condition that the vehicle is used to generate, assure and maintain taxable income.
- In case the vehicle is not used solely for business purposes, the lump sum will be decreased to CZK 4 000. For such a vehicle only 80% of tax depreciation can be claimed as a tax-deductible expense.
- In order to prove the purposes for which the vehicle is used, a taxpayer confirmation will suffice until the contrary is proved.
- One tax payer is entitled to claim expenses as lump sum for a maximum of 3 vehicles.

### Administration of Taxes Act: Enforcement of tax payers' rights

- Compared to the current wording according to which the reasons for decisions made during tax proceedings do not have to be given (except for situations stipulated by the law), the amendment implements an obligation for the tax authority to justify its decisions (in case this obligation is not explicitly precluded by the law). The reasons that led the tax authority to their decisions and the proof that supported their final conclusions should be apparent from future tax decisions.

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- The amendment implements the so-called suspensory effect of appeal, which was filed against the payment assessment resulting from a tax audit. This means that in case a tax payer files an appeal against additional tax assessment, the additionally assessed amount will be due only based on rejection of this appeal (and not after issuance of the additional payment assessment).
- This amendment is a response to a recent judicial decision of the Constitutional Court and explicitly confirms that it is not allowed to assess a tax liability after the lapsing of 3 years from the end of the taxable period in which the liability arose or after 3 years since the tax liability arose for taxes for which the taxable period is not applicable.

### Polite officers - new Tax Administration Code heading to senate

The Parliament approved a draft of a new Tax Administration Code, which should replace the current Administration of Taxes Act starting 2011. In the tax practice, the latter is considered obsolete and unsatisfactory.

According to the new Tax Administration Code, a tax authority will be obliged to avoid any impoliteness during tax proceedings and must accommodate the tax payer's needs as much as possible. We will have to wait for an evaluation of the new rules in practice as the new Tax Administration Code still has to be approved by the Senate and authorized by the President. After that, we can only wait for its effective date and eventual amendments before the Act becomes effective.

We will update you on the progress of implementation of the Tax Administration Code.

### Electronic purses finally legal

Within the June legislative storm, the Senate also approved a new Payment Systems Act which entitles institutions other than banks to also run a payment system. However, the right to receive deposits from the public will remain exclusive to banks.

The Act further allows issuance of so-called electronic money which will be important namely for e-transactions. The new Act also has tax implications in the area of VAT in cases where it is required to apply VAT in the moment of payment. Information about the most important tax issues created by the new regulation of the payment system will follow in one of the next issues of this bulletin.

### The Senate also approved the following Acts and amendments:

- Amendment of the Income Taxes Act including an amendment of the Act on reserves
- Amendment of the Act on Social Security Contributions
- New Act on the Support of Economic Growth and Social Stability
- Amendment of the Commercial Code

All newly approved regulations are currently awaiting authorization by the President. We addressed the most important changes incorporated in these amendments in the Tax Flash issued on 15 May 2009.

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## Customs Electronic entry and exit summary declarations – postponed

To eliminate risks related to import and export the EU will require importers and exporters to provide Customs Authorities with pre-arrival and pre-departure information (electronic entry and exit summary declarations). These declarations should be filed before importing and exporting goods into and out of the EU so that Customs has sufficient time to make a risk analysis. Based on the risk analysis performed, the relevant Customs Authorities will decide which consignments of goods may represent a threat and may need to be examined, and which shipments can pass through without any examination.

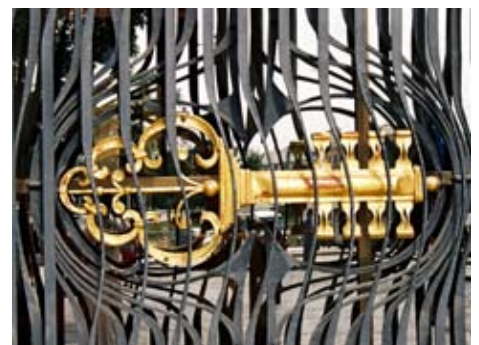
This obligation was due to become mandatory as of 1 July 2009. However, the Commission has decided that a longer transitional period is necessary to provide companies with sufficient time to make the necessary arrangements to be able to file the electronic entry and exit summary declarations. Therefore, a new regulation has been adopted.

Based on this new regulation, the transitional period will be from 1 July to 2009 to 31 December 2010. Companies can file electronic entry and exit summary declarations within this period, but it is not obligatory to do so. Customs will perform risk analysis based upon information available. Companies will be obliged to file summary declarations from 1 January 2010.

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## ... ECJ Corner

### RLRE Tellmer Property s.r.o. – Cleaning services subject to VAT

The European Court of Justice („ECJ“) has heard its first Czech VAT case. The case concerns whether separately itemised charges made by a landlord for the services of cleaning common areas of a residential apartment block fall within the VAT exemption for supplies of leasing or letting of immovable property. The ECJ has held that such cleaning services constitutes (in this particular case) a separate supply which does not fall within the VAT exemption for property letting when invoiced by a landlord to tenants separately.

The ECJ has restricted its judgment to the particular circumstances of the Taxpayer in this case – Tellmer Property s.r.o. - and, therefore, the judgment does not necessarily mean that such services must always be subject to VAT; it will depend on the facts in each case.

If the circumstances are different to those in the Tellmer Property case, e.g. the cleaning is not separately invoiced, or the rental contract includes the cleaning services, it may be necessary to consider the principles concerning single. v. multiple supplies to determine the correct VAT treatment. Businesses which let property should urgently review the current treatment of associated services provided in connection with letting to ensure that they are treated correctly for VAT purposes.

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## Excise duty – EMCS postponed

With respect to the new general Council Directive related to Excise Duty<sup>1</sup>, electronic administrative documents will be introduced from 1 April 2010. These electronic messages are intended to replace current paper-based Administrative Accompanying Documents (AADs). The electronic data exchange will take place under the Excise Movement and Control System (EMCS).

Since certain Member States are not yet prepared, the Member States of dispatch may continue to allow the movement of excise goods under the duty suspension arrangement covered by AADs from 1 April 2010 until 31 December 2010.

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<sup>1</sup>Council Directive 2008/118/EC

## Application of a new IFRS 8, Segment reporting

IFRS 8, operating segments has been replaced IAS 14 segment reporting and is effective for periods beginning on or after 1 January 2009. In this article you can familiarise yourself with the main changes introduced by IFRS 8.

IFRS 8 outlines requirements for segment reporting disclosure. It applies to entities preparing separate or consolidated IFRS financial statements and whose shares or debt securities are traded in a public market or are in the process of filing.

An operating segment is a component of an entity that earns revenues and incurs expenses and whose financial results are regularly reviewed by the entity's chief operating decision maker (either an individual or a body of the entity) to make decisions about the allocation of resources and assessment of performance. Under IAS 14, identification of operating segments was based primarily on a business unit and geographical basis. Under IFRS 8 the identification of operating segments may not result in different segments because the business unit or geographical basis used before may correspond with the new reporting format based on internal management processes. The base for segmentation must be disclosed (e.g., segmentation based on differences between products and services, geographical segmentation, combination of factors, etc.).

IAS 14 required the measurement of segment amounts based on IFRS accounting policies used in an entity's financial statements. Under IFRS 8, segment items are disclosed as reported in the internal management report to the chief operating decision maker. All segment information has to be reconciled to totals included in the entity's financial statements. All material reconciling items resulting from different accounting policies have to be explained.

Under IFRS 8, the component does not need to generate the majority of its revenue externally to be considered as a reportable segment. This change may result in additional segments being disclosed under IFRS 8.

IFRS 8 requires the disclosure of information on transactions with major customers. If revenues from transactions with a single customer, or a group of entities under common control amount to 10% or more of the reporting entity's revenues, the entity should disclose this fact as well as the total amount of revenues from each such customer and identity of the segments that generate the revenues.

The new IFRS 8 should make the preparation of the segment reporting of information easier. Users of IFRS financial statements should receive high quality information about profits, risks and the financial position of the company enabling them to make proper investment decisions. Comparative figures for prior year have to be restated in line with the new guide when IFRS 8 is adopted, unless the necessary information is not available and the cost to develop it would be excessive.

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## Amendment to Act on Protection of Economic Competition – considerable extension of the period for imposing a fine

As of 1 September 2009 an amendment to the Act on Protection of Economic Competition has become effective. The fact that new wording of the Act significantly extends the period the Office for the Protection of Economic Competition has for imposing fines for respective offences was only partly mentioned in discussions regarding the changes brought by this amendment.

The previous wording of the Act stipulated that the Office was authorised to impose a fine at the latest within three years from the day when it learnt of the offence, but at latest within ten years of the day when the breach of prohibition or failure to fulfill an obligation occurred. For instance, if there were delays in proceedings commenced by the Office a situation occurred in which even though it was decided that the offence was committed, it was no longer possible to impose the fine because the above-mentioned three-year period had elapsed.

In this respect the amendment brings a considerable change to the existing Act. From the moment the Office learns about an offence, it imposes a longer, five-year period. Moreover, the Office is not obliged to impose the fine within this time-limit; rather, it is sufficient if it only commences the respective proceedings. The length of the second time-limit running from the moment the offence is factually committed remains unchanged, i.e., ten years.

The argument presented to support the above-mentioned change is that it is difficult to discover unfair competition, to sufficiently procure probative evidence and to issue a decision within a three-year period.

From 1 September 2009, the only security against potential delays on the side of the Office thus remains a ten-day period running from the moment the offence is committed. The question is whether this time-limit in a dynamic competitive environment does not substantially interfere in the legal certainty of competitors.

For more information on the Amendment to Act on Protection of Economic Competition, please contact:

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## Criminal prosecution for economic results?

### Report from the seminar

The economic crisis has made managers of a number of companies face new challenges. After years of increasing profits they are presenting negative results to their shareholders, and are scrutinized by their company's owners, regulators and other involved entities. Thus, the risk that a manager will have to confront accusations has significantly increased compared to previous years. This can also be seen in connection with management meetings, which are considered to be more or less standard.

A professional seminar organised on Tuesday, 16 June, by Ambruz & Dark law firm in co-operation with PricewaterhouseCoopers (PwC) tried to reply to the question of how to prevent such risks. Sixty participants from among the management of prominent national companies took part. The main speaker, Jan Spáčil from Ambruz & Dark, together with his colleagues from PwC, David Borkovec and Jiří Urban, dealt with the following topics:

- Economic results and management's responsibility
- Where does criminal liability begin and what consequences can arise from a failure to adhere to management's obligations?
- Real examples of management's criminal liability
- Tax aspects
- Liability insurance

At the end of the seminar, the topic of possible preventive steps and measures to considerably decrease the risk of potential problems or even of criminal prosecution was also addressed. Among other things, the following measures were mentioned:

- Due legal treatment and documenting of all transactions and legal relationships
- Transparency
- Quality of process management in the company (Risk Management, Personal Data Protection, Internal Control, Corporate Governance)
- Professional standpoints on problematic/controversial transactions
- Taking into account and considering possible criminal consequences



## Comments from our professionals on current situation

### Conditions on the job market have become even harsher

The first half of 2009 was rich in data on the Czech job market. According to the Czech statistical office, the average salary rose by 3,1% to 22 328 kc in the first quarter and the real salary increased by 1%, the lowest increase since 1998.

The average salary stagnated in comparison with the trends of previous years. For the Czech Republic two salary adjustment periods are typical, i.e., the beginning of the year and 1 April. Reporting occurs at these times of the year in line with accounting and result consolidation periods of parent companies.

Whereas in the past years the salary increases were around 5%, this year's pay raise is negligible or zero. Over 60% of Czech companies enforced benefit freezes or even started with cutbacks. On the other hand, not all industries were significantly hit by the economic crisis and some industries will give pay raises to its employees as usual. However, salary increase across all industries will not exceed 1,7%, according to our research.

The Ministry of Labour and Social Affairs noted a slight growth in the number of unemployed during the month of May, which means a flat development of 7,9%. In the year to year comparison, this rate represents a significant increase. The unemployment level was at 5% last year.

Unemployment should be examined in the context of the Czech Republic workforce, which totals 5 million people. Another aspect which may not be evident at first sight is contract termination of agency workers who are not Czech citizens. A consideration of all these factors may point to a much higher impact on unemployment in the Czech Republic or, to a broader extent, across the CEE region.

While in the past manual workers or administrative staff was laid off on a larger scale, these days we also see managers and experts being dismissed. This phenomenon will have an impact on "salary inflation", which may, in comparison with previous periods, slow down and may cause employees currently searching for a job to be open to compromise in remuneration demands.

Branislav Hunčík, Manager, Human Resource consulting, PricewaterhouseCoopers Czech Republic

## The 10 most important trends in development of the pharmaceutical industry over the last 10 years

Specialization, a less aggressive style of marketing and cooperation instead of M&A are some of the main features that will become characteristic of the pharmaceutical industry in the upcoming period according to a PricewaterhouseCoopers survey called **"Pharma 2020: Which path will you take?"**

The survey also revealed that the global market with pharmaceuticals will double to 1,3 trillion dollars. The new model of pharmaceuticals will bear the following main attributes:

1. A more sophisticated direct-to-consumer distribution channels will diminish the role of wholesalers.
2. The benefits of cooperation within the industry will suppress the need of M&As
3. The nature of cooperation of pharmaceutical companies with other institutions ranging from research organizations to competitors will change
4. R&D will become more efficient – the "virtual patient" will bring cost savings
5. The blockbuster sales model will disappear; more emphasis will be placed on specialized medication and treatment procedures
6. Patient as well as the payer of medical expenses will gain more importance
7. Patients undergoing prescribed treatment will be under more consistent control
8. Focus will shift from treatment to prevention
9. International regulatory bodies will strengthen their positions
10. Emerging markets will reinforce their activity in the pharmaceutical industry

We have Published four studies from the **"Pharma 2020: Which path will you take?"** series. You can review and download all of them from our homepage-[www.pwc.cz](http://www.pwc.cz) in the publication section.



## Transform Magazine - New frontiers: Pulling ahead with innovation

Transform is PricewaterhouseCoopers' quarterly magazine for Central and Eastern Europe (CEE), covering the latest business trends in 25 markets across the region, from the Czech Republic to Kazakhstan.

The current issue of Transform Magazine focuses on innovation across the region. We are currently seeing a pattern across the territory in which each country is showing signs of strength in their own particular industry, whether it's the Czech Republic specializing in IT and software development, Poland finding its strong spot in health care research, or Russia leading nanotechnology development. What ensures fast progress and the establishment of technological hubs is development and an entrepreneurial spirit combined with a well-educated population in the CEE region.

In addition to the main theme of the publication, an article on Female institution also deserves attention. In the form of short stories, several remarkable female business leaders are introduced sharing secrets of success in their professions.

You may find and download the full version of the Transform magazine from our web-site – [pwc.com/transform](http://pwc.com/transform).



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