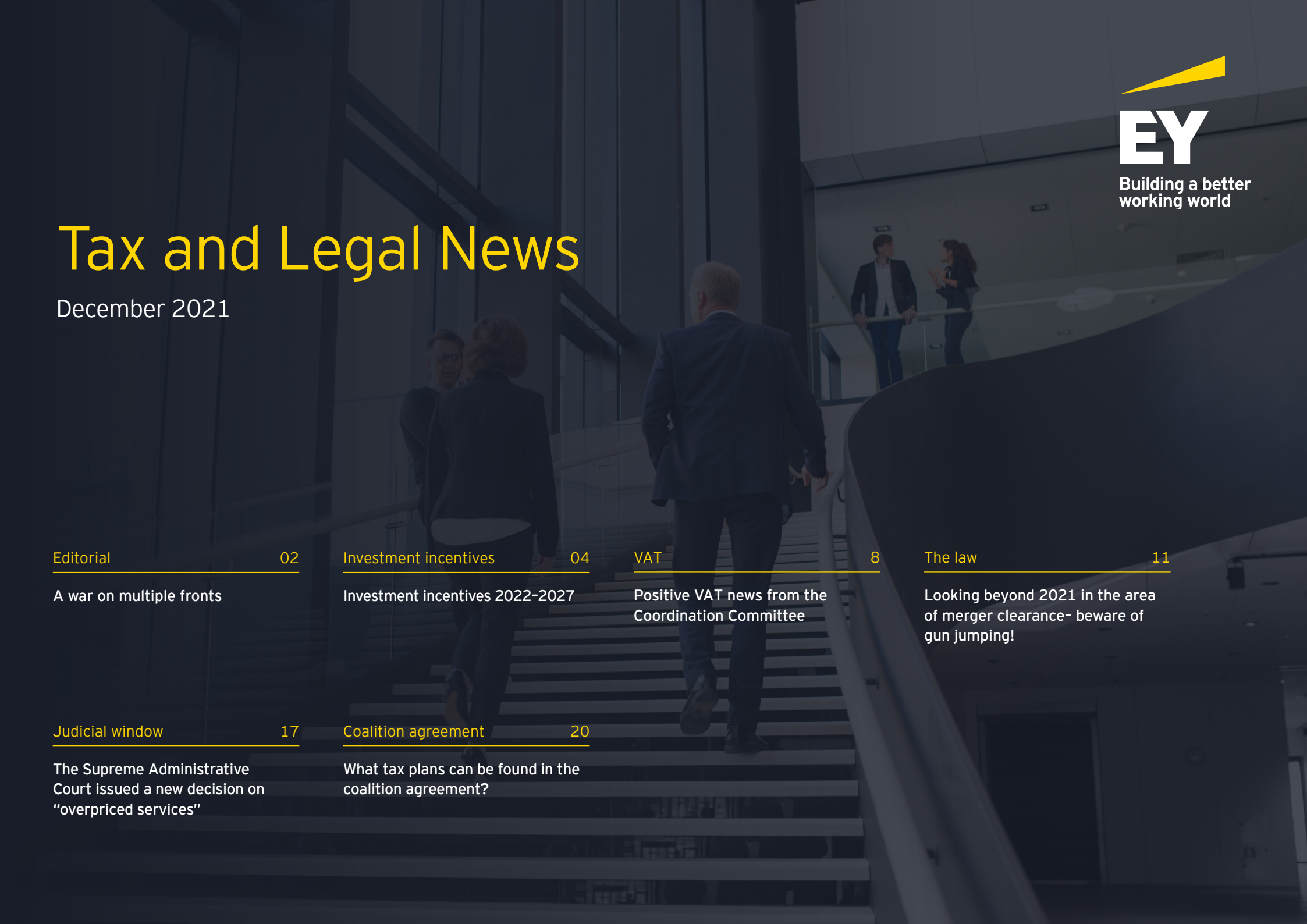

Building a better working world

Tax and Legal News

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A war on multiple fronts

The Supreme Administrative Court (SAC) issued a long-awaited decision in the case of a pharmaceutical company that had purchased and sold medicines purchased from its group on the Czech market (with Czech VAT applied). At the same time, it provided marketing services to the group (with no Czech VAT applied). It had to, otherwise it would have made a loss thanks to price regulation. The tax authority assessed Czech VAT on services because the services were – in their view - an integral part of the main supply, the sale of goods. The SAC annulled the assessment. Big victory. For the given pharmaceutical company, no question. Certainly good news for the rest of the pharma market, too. For other industries with similar alignments, it's hard to say.

At the outset is the unfortunate coexistence of price regulation and tax rules. The distributor must sell at a loss or violate price regulation. So it buys and sells at a loss. However, if it makes a loss, the tax authorities will charge transfer prices. So, it has to use some kind of adjustment. Maybe a marketing service. And it's forced to claim that the service is part of its business and overall profitability, and therefore that the transfer prices are fine. The more transfer pricing is okay, the more it will lead the tax authorities to believe the services are actually an integral part of the supply of goods and subject to VAT. It's a balancing act between three risks, a roulette game of whether there will be penalties for price regulation violations, transfer pricing violations or VAT violations.

In this case, the tax administrator opted for VAT and tried to claim that everything is one big supply to the customer – even the marketing service is provided to the end customer. Now, after reading the SAC judgment, this seems naive. Although the customer is the target of the marketing effort, he is certainly not the one to whom the marketing service would be provided. Perhaps naive in today's optics, but it made perfect sense to the tax authorities in both instances and to the regional court. Moreover, the taxpayer had shown that he was actually doing some general marketing and not necessarily just marketing for the goods he was distributing.

The question is what happens when a slightly less naive tax administrator comes to someone who's documentation of the services provided isn't as robust and/or doesn't provide separable marketing services for products other than those they distribute. And if I let my imagination run wild, I also see those who didn't bother with the service and just pay some kind of compensation or bill a content-free "transfer pricing adjustment". I think then the tax authorities might not even bother with the sophisticated "integral part of the main supply" and simply say the substance is a payment from a third party for goods subject to VAT.

It will be even more interesting in models where the group does not sell anything to the Czech subsidiary and just tells it what to produce and what to sell to whom and for how much. At the end of the year, it either takes a chunk of the profit (because it arranged the business) or, on the contrary, compensates for the losses (because it forced its subsidiary to sell to the group's major customers below cost). A perfectly working transfer pricing model with a completely bulletproof transfer pricing study. However, knowing the above-mentioned court case, it would not be surprising if the tax administrator were to come to collect VAT from the loss compensation. Here, it could try to argue that the service is not very separate and nicely tie it to the supplied goods.

In the opposite scenario, where the excess profit is subsequently transferred to the group, the tax authorities could then say they won't waste their time with VAT and just say it's a distribution of profit, which is a priori not deductible for income tax. This could be offered in particular in "profit split" transfer pricing models where the name itself suggests that it is a (non-tax deductible?) profit transfer.

Only practice will tell which end the tax administrator will grasp. There are counter-arguments, of course, but something will have to fund all the planned tax breaks in the coalition program...

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Investment incentives

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Investment incentives 2022–2027

With the end of 2021 just around the corner, let's have a quick refresher on what's in store for investment incentives from 2022.

Amount of aid

The amount of aid for large enterprises will now range from 20% (15% from 2025) to 40%, depending on the location of the investment. The aid amount will, as a rule, be increased by 20 percentage points for small enterprises and 10 percentage points for medium-sized enterprises. The highest amount of aid for large enterprises (40%) will be available in the Karlovy Vary and Ústí nad Labem regions, while support of 30% will be available in the Liberec, Hradec Králové, Pardubice, Olomouc, Zlín and Moravia-Silesia regions. In the remaining regions, aid will be 20% (15% from 2025), except in selected districts adjacent to regions with higher aid amounts, where 25% support will be available.

The above values will apply from 1 January 2022 to 31 December 2027. If the Just Transition Fund is approved, it should be possible to increase aid in selected regions for selected projects by 10 percentage points. In this case, however, the Czech Republic will need to submit a new regional aid map to the European Commission for approval.

Should the eligible costs exceed EUR 50 million and at the same time not exceed EUR 100 million, the aid intensity for the amount exceeding EUR 50 million will be reduced to half of the default values mentioned above. If eligible costs exceed EUR 100 million, aid can only be granted after approval by the European Commission (individual notification) – aid for costs exceeding EUR 100 million would then be set at 34% of the standard aid amount.

Supported activity

In regions with 20% aid (15% from 2025), only investments in new economic activity (i.e. no longer expansion projects) will be eligible for new support for large enterprises.

Investment in tangible and intangible assets to set up a new establishment or to extend the range of activities of an establishment will be considered a new economic activity, provided the new activity is not the same as or similar to that previously carried out in the establishment. The same or similar

activity will be assessed according to the four-digit classification of economic activities code (CZ-NACE codes).

Easier availability of material aid for the acquisition of tangible assets?

Manufacturing

Subsidies for the acquisition of tangible and intangible fixed assets for strategic investment projects in manufacturing could newly be more accessible to a wider range of investors. In selected regions, the subsidy could reach up to 20% of the total eligible costs (Karlovy Vary, Ústí nad Labem and Moravia-Silesia regions). In other regions, the maximum value of material support for the acquisition of tangible and intangible fixed assets should remain at 10%.

Recall that 'preferred' strategic investment actions in manufacturing that are not required to meet the conditions of investment value and job creation (see conditions below) already include such actions, where the object of production is a **product of strategic importance for the protection of life and health of persons** (various medical devices, appliances, medicinal products, etc.). At present, it's possible to obtain a subsidy for the acquisition of assets for these types of manufacturing projects in the amount of 10% of the qualified costs (maximum CZK 1.5 billion).

The new 'preferred' manufacturing activities described above should be further expanded to include investments carried out in manufacturing industries with high technological intensity and in higher value-added activities, where research and development is carried out using key enabling technologies **such as advanced materials technology, nanotechnology, advanced manufacturing technology, biotechnology, photonics, microelectronics, nanoelectronics and artificial intelligence technology.**

For other strategic investments in manufacturing (not falling into the above-mentioned preferred categories), the conditions for obtaining subsidies for the acquisition of assets should be adjusted – specifically, the minimum required value of the investment should be increased to CZK 2 billion (previously CZK 500 million), the minimum value of machinery to CZK 1 billion (previously CZK 250 million) and the minimum number of new jobs reduced to 250 (previously 500).

Technology and repair centres

For the sake of completeness, we add that investment in a technology or repair centre qualifies for a subsidy of up to 20% of the total eligible costs (maximum CZK 500 million) if the conditions are met. The conditions for obtaining subsidies for technology/repair centres, namely investment in assets of CZK 200 million (of which at least CZK 100 million in machinery) and the creation of at least 70/100 new jobs remain unchanged.

The amended regulation regulating the conditions under which material support for the acquisition of property will be newly granted has already been approved by the Government and should thus come into effect on 1 January 2022.

Investment after 1 January 2022

If you plan to invest at least CZK 80 million (CZK 40 million in selected regions), or your investment is directed to one of the preferred activities described above, it may be very interesting to apply for an investment incentive after 1 January 2022 – newly, in addition to the tax rebate, you may qualify for a subsidy of up to 20% for the acquisition of tangible assets.

If you have any questions, please contact either the authors of the article or your usual EY team.

Aid for large enterprises will range from 20% (15% from 2025) to 40% of the value of qualifying costs from 2022. For many projects in manufacturing, it's already easier to obtain a subsidy for the acquisition of tangible assets (10% of qualifying costs) without having to fulfil the higher value added condition. In addition, the range of qualifying projects will be extended from 2022 and the possible material support will increase to 20% in selected regions.

VAT

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Positive VAT news from the Coordination Committee

In this article, we provide a summary of two positive contributions from the Czech Chamber of Tax Advisors Coordination Committee ("CC"), both from EY submitters.

586/15.09.2021 Adjustment of the tax base after clawback payments to health insurance companies (Ing. Martin Novák, Ing. Tomáš Synák)

This CC addresses a situation that often arises in practice in the pharmaceutical business. Health insurance companies require the holder of a marketing authorization for a particular drug (the so-called "MAH") to enter into a cost limitation agreement with the insurance company and, on the basis of such an agreement, to reimburse the insurance company for the so-called clawback payments for drugs. The MAH is often a foreign company that distributes the drug in the Czech Republic through other local entities (usually from the same group) and does not sell the drug itself. The repayments required by the insurance company are usually economically borne by the local distributor (Czech s.r.o.), which often acts as a representative in the contract with the insurance company.

It was clear from the previous interpretations that if the contract with the insurance company was concluded directly by the local distributor in the capacity of a standard contracting party, then it could correct the tax base for the supplied medicines according to § 42 of the VAT Act. However, it has not yet been made clear whether a local distributor who pays the clawback payments but is not a direct contractor to the insurance company can do the same.

The GFD in its opinion on the CC has now confirmed that in the second case it will also be possible to correct the tax base of the supplied medicines. The Czech distributor must be named as an agent in the contract to limit the risks associated with the reimbursement of the medicinal product or otherwise agree to the MAH's obligations in an appropriate manner.

In practice, the specific mechanism for correcting the tax base will need to be thought through and the time limits for correction will need to be monitored. Our team has practical experience in this and will be happy to assist you.

589/24.11.21 Application of VAT on the right to build (Ing. Stanislav Pokorný, Ing. Jevgenija Bajzíková)

The right to build is a relatively new concept in Czech legislation; therefore, many problems still arise in practice with its legal and tax treatment. The VAT Act contains a fiction according to which the right to build is considered as goods. In general terms, this means that at the outset it should be taxed as a lump sum (a supply of immovable property) on the sum of all future construction payments. However, this approach poses problems when future construction payments change over time (e.g. due to indexation) and it is not possible to determine the tax base at the outset. There is no special mechanism in the VAT Act for the right to build to correct the tax base after three years.

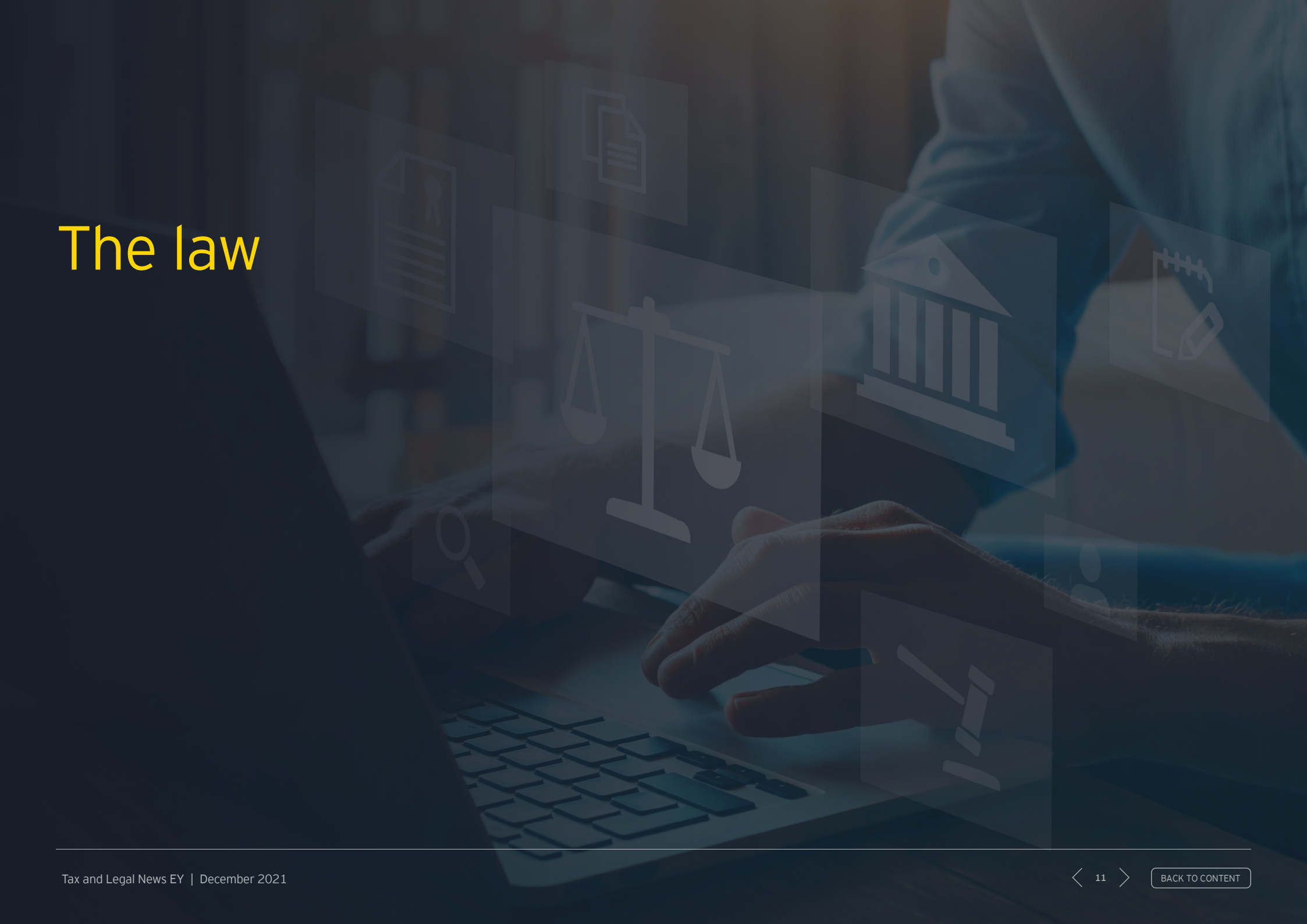
The GFD confirmed the drafters' proposals that in the case of a suitable contractual setup (e.g. in the form of partial supplies), the right to build could be taxed by VAT continuously with each construction payment. The method of taxation (VAT rate, VAT exemption, reverse charge) should be determined taking into account the state of the land/building at the outset.

For companies that are going to establish the right to build, we recommend to set up the contract documentation in advance. Our team has practical experience with this and will be happy to assist you.

If you have any questions, please contact either the authors of the article or your usual EY team.

For companies that are going to establish the right to build, we recommend setting up the contractual documentation in advance.

The law



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Looking beyond 2021 in the area of merger clearance – beware of gun jumping!

One area of law in which it is important to follow the decisions of the European Commission and the judicial authorities of the European Union (EU) is competition law, in particular the area of merger clearance. Decisions of EU institutions in this area of law can also have a significant impact in private law transactional relations. A number of such decisions has also seen the light of day during 2021. Regarding merger clearance, this year was particularly rich in decisions focusing on breaches of the obligation to obtain regulatory approval prior to a given merger. Two of these decisions are discussed below.

The European Commission's decisions in this area are also important in that national competition authorities often follow these decisions in their own decision-making practice. They are therefore also worth monitoring.

Mergers – a brief introduction

A merger between two or more competitors operating in the same market is subject, in some cases[1], to the approval of the national competition authority, which in the Czech Republic is the Office for the Protection of Economic Competition (Office). Where the merger is of pan-European significance[2], it is subject to approval by the European Commission.

The concept of merger of competitors must be viewed broadly – it is not only a situation where one company acquires its competitor, but also the establishment of a joint venture, the transfer of a business, in

1 The criterion for assessing whether or not a transaction is subject to approval is achievement of the prescribed turnover levels set out in the Competition Act – each of the parties to the transaction must have a turnover of at least CZK 250 million and the cumulative turnover of all participants must reach at least CZK 1,500 million.

2 The decisive criterion is again turnover – at least two of the parties to the transaction must have an EU-wide turnover of at least EUR 250 million and the cumulative worldwide turnover of all parties must be at least EUR 5,000 million.

general, any situation where an entity acquires direct or indirect control over its competitor (see, for example, the decision in Altice v. European Commission, described below).

In such a case, before the transaction is settled, the relevant competition authority must be informed, and will then issue a decision approving or rejecting the merger. No merger can be carried out without approval (this is known as the standstill obligation). A situation where a merger is implemented prior to notification/approval by the relevant competition authority is known in the professional community as "gun jumping". A situation where a merger is implemented before the competition authority's approval is given can be compared to a 100m race where one of the participants "takes off", i.e. runs out of the starting blocks without being instructed to do so by the starter in the form of a shot from the starting gun.

Gun jumping can result in a fine of up to 10% of the competitor's net turnover for the most recently completed financial year. In the event that the merger is implemented without the approval of the competition authority, measures necessary to restore effective competition in the relevant market may be imposed – in particular, an obligation to sell the subject of the transaction or to cancel the contract on the basis of which the merger was implemented.

Altice decision – definition of contractual arrangements constituting gun jumping

Altice Europe is a French company with an international presence in telecommunications and mass media. In September 2014, it signed a sale and purchase agreement (SPA) with Brazilian telco Oi to acquire PT Portugal (the largest telco in Portugal) from Oi.

The SPA contained "pre-closing covenants", provisions that take effect prior to the settlement of the transaction and give the buyer certain powers in relation to the target company. Pursuant to these provisions, Altice's approval was required for (i) the appointment and removal of PT's senior management, (ii) the modification of PT's pricing policy, and (iii) the approval to enter into, modify or terminate any material contracts, regardless of whether such action would have any effect on the maintenance of PT's value. In accordance with the SPA, Altice used its powers in several cases (e.g. to interfere in PT's marketing policy).

The European Commission was notified and approved the transaction in April 2015.

However, in March 2016, the European Commission launched an investigation into whether the inclusion of pre-closing covenants in the SPA resulted in the transaction being implemented prior to approval by the European Commission.

The European Commission concluded that Altice's conduct breached both the notification obligation and the obligation not to implement the transaction without prior approval from the European Commission, for which it imposed a fine of EUR 124.5 million. According to the European Commission, Altice was able to exercise control over PT by means of the powers granted by the SPA (the aforementioned pre-closing covenants). In the European Commission's view, Altice thus implemented the merger before the transaction had been approved by the European Commission and partly even before the transaction had been reported.

Altice challenged the European Commission's decision before the EU General Court, which, however, upheld the European Commission's decision (only reducing the imposed fine).

In its application, Altice stated that the purpose of the pre-closing covenants was to preserve the integrity of economic activities in the period between the signing of the SPA and the settlement of the transaction. However, the EU General Court did not find this objection to be well-founded. According to the EU General Court, similar arrangements which

give the buyer the right to interfere in the commercial affairs of a target company are permissible (authors' note – they are also quite common in transactional practice), but only to the extent that their purpose is to preserve the value of the target company. The assessment of whether a particular provision is necessary in order to preserve the value of the target company or whether this limit has already been exceeded will vary from case to case and it is not possible to categorise individual provisions (with exceptions) in a clear way.

For example, the SPA contained an obligation to seek Altice's consent to the appointment of any member of PT's governing body (similarly, Altice's consent was required to terminate or amend their service agreement). According to the EU General Court, the possibility to co-determine senior management positions without any restriction is in itself a possibility to exercise control within the meaning of competition law (with the associated obligations), i.e. there is always a de facto acquisition of control.

On the other hand, in its judgment, the EU General Court gives some guidance on how to ensure that the value of the target company does not drop between the conclusion of the SPA and the settlement of the transaction, so that at the same time the relevant provisions comply with EU competition law. For example, according to the EU General Court, it is permissible to restrict the possibility of personnel changes in relation to employees of the target company that would have a significant impact on the company's cost base, or to restrict the possibility of terminating cooperation with key pre-designated employees of the target company.

Another provision which, according to both the European Commission and the EU General Court, went beyond what was necessary to preserve the value of the target company was the obligation for PT to seek approval for the conclusion of any contracts the subject matter of which exceeded EUR 5 million in aggregate or which Altice would have found to be significant irrespective of their value. The EU General Court has not categorically rejected a similar type of provision in this case either. However, any financial criteria must be set in such a way as to show that they are intended to ensure the value of the company is preserved. The financial criteria for the approval of contracts must therefore not be unreasonably low, particularly in view of the value of the transaction or contracts that the target company normally enters into.

According to the judgment of the EU General Court, gun jumping constitutes the very possibility of exercising decisive control. It is not necessary that the exercise of control actually take place (though in the case of Altice it did). In practice, this means the mere existence of the above-mentioned problematic provisions in the SPA will amount to gun jumping, regardless of whether the buyer actually exercises any of its powers.

Gun jumping is also sanctioned by the Office for the Protection of Economic Competition in its current decision-making practice. In 2020, it imposed a fine on a Czech company[3] in an amount of roughly CZK 4.5 million for, inter alia, exercising its right under the acquisition agreement to make a binding proposal to the seller to replace the directors of the target company (which the seller respected). The company benefited from a settlement procedure, which resulted in a 20% reduction of the fine.

Article 22 of the EU Merger Regulation – a new weapon in the hands of the European Commission?

Article 22 of the EU Merger Regulation (EUMR) has recently entered the spotlight of European competition law and M&A experts. This was due to the European Commission's approach taken in the case of the acquisition of GRAIL, a US company developing technologically-advanced cancer detection tests, by Illumina, another US company also active in the healthcare sector.

3 The same company was fined once more for gun jumping in the same year by the Office, again with a fine of approximately CZK 4.5 million.

The acquisition was not reported to any of the national European competition authorities (and therefore not to the European Commission) as the relevant economic criteria were not met in any country. Thus, it was not even necessary to obtain the approvals of the competition authorities concerned for the transaction. Neither GRAIL nor Illumina has any significant business activity in the EU – for now – although future activity in the EU can be expected. At first glance, this would appear to be a smooth transaction from a competition law perspective in the EU.

Article 22 of the EUMR[4] provides that one or more Member States may request the European Commission to review any merger (transaction) that is not EU-wide (i.e. does not meet the prescribed worldwide turnover criteria) but (i) affects trade between Member States and (ii) threatens to substantially impede competition in the territory of the Member State or States making the application. The European Commission itself has recently invited Member States to refer certain specific cases to it under Article 22 of the EUMR. Evidently, then, we will see more cases like this in the near future. In the case of Illumina's acquisition of GRAIL, several European competition authorities have done so, apparently on the basis of information they received about the transaction from the media. Following this request, the European Commission has opened an investigation into whether the proposed transaction is compatible with EU competition law. Subsequently, Illumina itself reported the transaction to the European Commission (presumably in view of the ongoing investigation). However, as mentioned above, a transaction that is subject to notification and subsequent approval by the European Commission cannot be implemented without the approval of the European Commission (standstill obligation). Nonetheless, Illumina subsequently completed the transaction despite the fact that the European Commission had not yet approved it.[5] Thus, in the eyes of the European Commission, a breach of the standstill obligation occurred. In response, the European Commission took the unprecedented step of imposing interim measures. On this basis, GRAIL must remain a separate entity (i.e. there can be no merger with Illumina), it must have independent management, GRAIL and Illumina must not exchange confidential information of an economic nature and their business cooperation should respect the arm's-length principle. In addition, there is a threat the European Commission will impose a fine on Illumina for violating its obligation to report the transaction and not to implement it before approval. In the most extreme case, the European Commission may conclude that the transaction would be anti-competitive and order the parties to cancel the transaction.

Article 22 of the EUMR and the current decision-making by competition authorities and the European Commission thus introduces considerable uncertainty into European transactional practice. As the criteria for the application of Article 22 of the EUMR are very vaguely defined, almost any major transaction (especially in a sensitive area such as pharmaceuticals or information technology) potentially finds itself in the crosshairs of the European Commission.

In March 2021, the European Commission issued official guidance on the application of Article 22[6], which provides at least basic application guidance in which the European Commission, among other things, goes into more detail on the definition of companies in the relationship for which the application of Article 22 of the EUMR could possibly be considered (in addition to the aforementioned pharmaceutical and IT sectors). It specifically mentions undertakings:

a) with significant competitive potential that have not yet developed or implemented a business model generating significant revenues;

4 For the sake of completeness, we add that Article 22 of the EUMR was originally intended to serve as a competition protection tool in cases where a Member State did not yet have its own national merger control regime. However, in view of the development of merger control legislation, this purpose is now obsolete.

5 Illumina has apparently done so on its own grounds that the standstill obligation applies only to compulsorily reported transactions, and will seek to enforce this argument in any court proceedings before the EU Courts.

6 Available here: EUR-Lex - 52021XC0331(01) - EN - EUR-Lex (europa.eu).

b) that are important innovators or carry out potentially important research;

c) that are an actual or potential significant competitive force;

d) that have access to competitively significant assets (e.g. raw materials, infrastructure, data or intellectual property rights); or

e) that provide products or services that are key inputs/components for other industries.

The spectrum of companies in a relationship for which the European Commission considers the application of Article 22 of the EUMR to be relevant is therefore extremely broad.

Article 22 of the EUMR is also problematic in terms of the time limit within which the transaction may be referred to the European Commission. The EUMR provides that the application must be submitted no later than 15 working days from the date on which the merger is reported or if no notification is required, otherwise made known to the Member State concerned. In particular, where no notification is required, it is questionable when the time limit starts to run.

Article 22 of the EUMR can thus be figuratively imagined as authority through which the European Commission can "pull in" quite a wide range of transactions. In view of current practice, it is therefore appropriate to approach transactions, in particular those involving the IT or pharmaceutical sectors, with the knowledge that the national competition authority may submit a request for an assessment of the transaction by the European Commission within the meaning of Article 22 of the EUMR, with all the ensuing consequences. In this context, we recommend above all that the transaction documentation take such a situation into account. Furthermore, it is advisable to consider a procedure whereby the transaction is pre-reported out of an abundance of caution in order to avoid the transaction subsequently being referred to the European Commission to the surprise of all parties involved.

If you have any further questions, please contact the authors of this article or other members of EY Law or your usual EY team.

For example, the SPA contained an obligation to seek Altice's consent to the appointment of any member of PT's governing body (similarly, Altice's consent was required to terminate or amend their service agreement). According to the EU General Court, the possibility to co-determine senior management positions without any restriction is in itself a possibility to exercise control within the meaning of competition law (with the associated obligations), i.e. there is always a de facto acquisition of control.

Judicial window

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The Supreme Administrative Court issued a new decision on "overpriced services"

Some years ago, cases of taxpayers purchasing services whose price, according to the tax administrator, was significantly above the market level ("overpriced services") began to appear in the case law of administrative courts.

The transactions were often between persons who were not related either financially or personally (or the tax administrator failed to prove this). At the same time, in some cases no other transaction related to the purchase of the "overpriced" services was proven, nor was the buyer's motive for purchasing the overpriced service (the mere purchase of an overpriced service at first sight is not economically rational for the buyer).

The tax administrator focused on similar transactions, for example, because the supplier of the service failed to pay corporate income tax (sometimes in combination with VAT) and the tax administrator was unable to recover this tax. The tax administrator therefore attempted to increase the tax base of the service recipient, arguing that the price of the service did not correspond to the arm's-length price, and that the buyer and seller were otherwise related persons under § 23(7)(b)(5) of the Income Tax Act because they created the legal relationship primarily for the purpose of reducing the tax base or increasing the tax loss. The conclusion of a contract for the provision of services may be regarded as a legal relationship.

There has been a long-running debate among the professional community as to whether the mere "inflating" of a price (and the conclusion of a contractual relationship for the provision of services) implies that the buyer and seller are related persons who entered into the relationship primarily for the purpose of reducing the tax base or increasing the tax loss, so that the tax authorities can adjust the prices of their transaction (for tax base purposes).

In its new decision, the First Chamber of the Supreme Administrative Court (SAC) briefly commented on some of the previous decisions on this issue and formulated conclusions regarding the application of § 23(7)(b)(5) of the Income Tax Act in the situation it was examining.

Regarding one of the previous SAC decisions[7], the First Chamber stated that in the case in question the price increase was quite obvious (e.g. a more than 200-fold price increase) and at the same time there were other suspicious circumstances (non-standard content of contracts, negligible benefit of advertising for the tax entity's activity, etc.).

7 Decision No. 7 Afs 176/2019-26

However, the newly considered case was different. The tax administrator did not allege suspicious circumstances and adjusted the tax base under § 23(7)(b)(5) of the ITA only on the basis of the high price for services. The First Chamber rejected such an approach and formulated that an adjustment of the tax base is only possible if the tax administrator cumulatively proves (i) that there were related parties and (ii) that the prices agreed between these parties differ from the prices that would have been agreed between independent parties in the ordinary course of business under the same or similar conditions.

The SAC pointed out that the tax administrator must prove that the legal relationship was actually created for the purpose of reducing the tax base or increasing the tax loss. If the price for the services was paid and at the same time it was not proven that the funds were returned to the customer, the payment of an overpriced service solely for the purpose of reducing the tax base would lack any rationality, as it would be financially disadvantageous for the customer. Therefore, the creation of a legal relationship cannot be automatically presumed.

With regard to another cassation objection concerning the comparable price (on the basis of which the tax administrator determines whether the price for the service is in accordance with the arm's-length principle), the SAC stated that the tax administrator cannot only use the price of renting advertising space as a comparable price in the case of a comprehensive advertising service. The mediation of the advertising itself (beyond the rental of advertising space) may represent an added value of the service.

We believe that the decision of the First Chamber of the SAC brings more legal certainty to the complex issue of § 23(7)(b)(5) of the Income Tax Act for taxpayers.

We will be happy to discuss this or other similar situations with you in more detail.

If you have any questions about the above topics, please contact the author of the article or your usual EY team.

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Coalition agreement

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What tax plans can be found in the coalition agreement?

The SPOLU coalition and the Pirates and Mayors coalition signed a coalition agreement that includes, among other things, a coalition program describing how the parties in the future governing coalition intend to govern the country (more in Czech HERE).

Below is an extract of the tax-relevant items contained in the coalition program:

Systemic

- We will create a tax brake rule that caps the tax burden. Once the composite tax quota reaches it, tax increases will automatically be ruled out.
- We're implementing real pension reform... The pension will consist of two main components and a third voluntary one. The basic guaranteed component, the amount of which should always reflect the requirements for dignity of life in old age and the financial possibilities of the state, will be increased. The merit component will be based on contributions to the system and the number of children raised. Third, voluntary component: analysis of the current effectiveness of third pillar support. Establishment of a state or public fund inspired by Sweden for voluntary savings over and above compulsory social insurance. In addition, voluntary private pension savings, for example in the form of a long-term investment account.
- In the European Union, we will push for transparent reporting of multinational companies according to the country of origin of revenues and limit the scope for illegal tax optimization at the expense of Czech citizens.
- We will support a minimum corporate tax in the EU and OECD to ensure that the profits of multinational corporations are taxed where they are earned.
- We will address the problem of dividend outflows abroad. We will favour reinvestment back into the Czech economy.
- We will crack down on tax evasion.

- We will ensure better measures against transfer pricing and illegal optimisation practices and tax evasion.
- We will examine the possibility of abolishing non-systemic tax exemptions.
- We will remove 'tipping points' from welfare and tax systems so that entitlements to tax credits and welfare benefits are as seamless as possible, people are more motivated to be active and not trapped in poverty.

Depreciation

- We will reduce the number of depreciation groups and shorten the depreciation period for selected ones.
- We will reduce the depreciation period to 20 years to motivate investors to build rental housing.
- We will reduce the depreciation period for other buildings (other than residential buildings) for investments with minimal consumption (photovoltaic panels on the roof, rainwater harvesting, heat pump for heating).

VAT/the environment

- We will increase the limit for compulsory VAT registration to CZK 2 million.
- We will motivate companies to operate in an environmentally-friendly way, and we will examine the possibility of reducing VAT on all environmentally-friendly products.
- Excise duties will take into account harmfulness.
- Municipalities, regions and the state will receive more money from the extraction of mineral resources on their territory thanks to the taxation of mining. We will also remember the adjacent communities.
- We will reduce VAT on the construction or reconstruction of flats and houses.
- We will create a central catalogue of recycled building elements and build "recycling hubs" to produce tax-efficient building materials from waste.

Work

- We will support part-time work by reducing social security contributions. We will set the conditions for tax credits and deductions in an incentive-based way with reasonable marginal tax rates.
- We will reduce social insurance on the employers' side by 2 percentage points, assuming consolidated public finances.
- We will introduce a wide range of part-time work options (including favourable taxation) and increase the overall flexibility of the Labour Code in the interests of both employers and employees.

Other

- We will introduce the indexation of taxpayer relief.
- We will introduce a tax holiday with income capping for families drawing parental allowance or having three or more children.

- We will introduce the possibility to deduct payments for care services from taxes (up to a certain limit).
- We will cut off companies using tax havens from public money.
- We will expand municipalities' options in setting the basic property tax rate coefficient.
- We will reduce the bureaucratic burden of tax and fee administration, abolish the EET and parametrically adjust the control report.
- We will introduce a single collection point through the development of the MY Taxes portal.
- We will enforce rules for transparent documentation of the beneficial owners of companies that receive subsidies, investment incentives and public contracts.
- We will push for permanent higher tax benefits for patronage and sponsorship as a step towards functional multi-source funding for culture.
- We will introduce the option to pay 1% of your pension insurance to your parents or grandparents.
- We will make it possible to keep accounting and tax records in euros.
- We will provide tax support for reinvestment in research.
- We will propose a voluntary joint assessment for spouses.
- We will reduce the time needed to qualify for a pension.
- We will return the standard period of study to a substitute period.
- All payments to the public administration, including revenue stamps, can be paid by credit card or cashless.
- We will introduce the option of voluntary supplementary health insurance.
- We will support cultural and creative industries, including systematic and sustainable support for the film industry through film incentives.

If you have any questions about the above topics, please contact the authors of the article or your usual EY team.

The coalition agreement includes, among other things, a coalition program that describes how the parties in the future governing coalition intend to govern the country – including tax plans.

For further information please contact either your usual partner or manager.

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ED None

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Did you know:

- The SAC published a landmark decision on the application of VAT on "price leveling"?
- There are tax pitfalls of a transfer pricing model based on compensation payments?
- A package of significant tax changes in Poland (most expected to take effect from 1 January 2022) was approved?
- Workplace COVID testing of employees is once again mandatory?
- EY is organising the seminar *Employees* in 2022?
- The public CbC reporting has been officially published?