20 October 2020

Indirect Tax Alert

Czech Government proceeds with legislation on Digital Services Tax

The Czech Republic (CR) has announced it will proceed with its plan to introduce a Digital Services Tax (DST).

The Czech Government decided to introduce a domestic DST following the delay in a unified approach at both the global (Organisation for Economic Co-operation and Development) and regional level (European Union). The Czech DST is expected to apply temporarily, until an international approach is implemented.

The draft law was approved by the Government and is currently being discussed in the second reading in the Chamber of Deputies (the legislative process has not been completed and the legislation may still be amended).[1]

Czech tax professionals are debating whether the proposed tax could in fact be levied in the case of entities from countries that have concluded double tax treaties with the Czech Republic. Indirect taxes normally do not fall within the scope of such treaties.

Under the proposed legislation, the following activities would be subject to the DST:

- Targeted ad campaign services
- Use of a multilateral digital interface
- Supply of user data

The payer of the tax should generally be a member entity of a group (or a standalone entity) that has provided a taxable service rendered during the base period, if the following four thresholds are met:

- Total (consolidated) revenues of the group (or standalone entity) for the base period are greater than €750 million
- The amounts of remuneration for the provision of taxable services for the base period by the group (or standalone entity) attributable to the CR is higher than CZK100 million for this group
- The amounts of remuneration for taxable digital services exceed 10% of the group's total revenues (within the European Union, European Economic Area and Switzerland)
- A minimum level of taxable activities per entity (amounts of several group entities providing the service jointly should be aggregated) has been in the CR:
  - A targeted ad campaign during the base period if the partial tax base from this taxable activity in that period is higher than CZK5 million;
  - Use of a multilateral digital interface during the base period whereby the total number of user accounts of this multilateral digital interface exceeded 200,000 in this period;
  - A supply of user data during the base period if the partial tax base from this taxable service in that period is higher than CZK5 million.

The draft law specifies allocation keys – generally derived from payments by Czech users or ratio of activities of Czech users compared to activities of all users – based on which the remunerations attributable to the CR should be calculated.

The proposed tax rate is 7% (there is an amendment to reduce the rate to 5%).

In line with the proposed amendment the DST would come into effect on 1 January 2021 (the original intent was mid-2020).

For the assessment as to whether the proposed tax could in fact be levied in the case of entities from countries that have concluded double tax treaties with the CR, it is important to determine whether the proposed tax qualifies as a direct (akin to income tax) or indirect tax. The Ministry of Finance states in the Explanatory Memorandum that the tax is indirect (regardless of profit and income). As a consequence, double tax treaties will have no impact on the proposed tax. The answer to this question may still be open to interpretation.

Endnote

1. You can monitor the legislative process here (in Czech): https://www.psp.cz/sqw/historie.sqw?o=8&t=658.

For additional information with respect to this Alert, please contact the following:

Ernst & Young, s.r.o., Prague

- Radek Matuštík radek.matustik@cz.ey.com
- Jakub Tměj jakub.tmej@cz.ey.com