Legal News II/2017

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Dear Clients and Business Partners,

Let me present to you another edition of Havel, Holásek & Partners’ Legal News.

Right at the outset, we would like to draw your attention to certain legislative changes in the area of taxes, which may affect the business environment in the Czech Republic. One of them should remove quite a significant tax obstacle that has so far put Czech trust funds at a disadvantage. Such trust funds (in Czech: svěřenské fondy) represent an institute that we consider – and our legal practice confirms as being – a suitable tool for long-term management of private wealth.

If you fill in tax returns in Slovakia, you will have noticed significant tax changes that came into force on January 1 this year. You can find a summary of these changes in our final article.

Our newsletter also includes two important amendments to Czech laws. The first one relates to the Companies Act and reintroduces the entitlement of employees to participate in the functioning of a joint stock company. The second one supplements the Act on Certain Anti-Money Laundering and Terrorism Financing Measures (the AML Act, or Anti-Money Laundering Act) and affects, among other things, the public procurement area.

This issue contains not only our partners’ and associates’ texts, but also brief information on our awards and certain significant transactions in which we have been involved, as well as an overview of upcoming seminars at the Havel, Holásek & Partners Academy to which you are warmly invited.

I wish you an interesting and useful read.

Jaroslav Havel
Our tax consultancy practice group is a part of the largest M&A practice group in the Czech Republic and Slovakia. The team of eight experienced tax lawyers provides a unique combination of legal expertise and knowledge, with regard to both national and international tax issues.

We are able to offer clients innovative solutions and identify opportunities for tax planning at the local and international level, owing to the availability of an extensive network of partner international tax specialists. Besides our primary focusing on tax and legal structuring, we provide comprehensive advisory services in all fields of tax law.

We are the most recommended law firm in the Czech and Slovak official Law Firm of the Year awards in the Tax Law category.

**Tax law advisory services**

- tax structuring of transactions (including acquisitions, divestments and mergers, private equity and venture capital funds)
- analysis of tax position when doing business in the Czech Republic and Slovakia
- holding and international structures with a focus on capital gains and dividend tax optimisation
- structuring of investments in immovable or intangible assets
- tax compliance in national and international taxation
- tax services to both private and corporate clients
- representation and consultation in on-site inspections, procedures to avoid doubts, and tax inspections under tax procedure rules
- representation of clients in disputes with tax and customs authorities and before administrative, civil and constitutional judicial bodies
- advising on taxation of individuals, labour costs, and tax deductions (including taxation of international employees, stock option plans and management remuneration)
- advising branches of foreign persons operating in the Czech Republic
- legal aspects of excise taxes, VAT and customs duties, organizational and technical requirements for payers of such taxes
- comprehensive legal advice on import, export an transit
The year 2017 brings tax changes and stricter property registration rules

This year ends the parliamentary term in which the Czech government has stipulated in its coalition agreement as one of its priorities, among other things, to improve tax collection, to minimise tax evasion, and to adopt a special law on proving the origin of property. The aim of the following summary is not to evaluate how successful the Czech government has been in its effort. After all, a number of legislative changes have come into effect only recently, or are in the preparatory stages, often tied to time limits for implementing EU law into Czech law. We summarise only several changes which we consider significant from the perspective of regulation of business environment in the Czech Republic, not only for the year 2017, but also for the upcoming period.

Trust funds – a possible exemption of received profit shares from Czech tax

Trust funds represent a very useful tool that is most often used for property distribution structuring within a family. The motivation for their establishing usually is to maintain a living standard of both parents and children, when money and revenues are used, for example, not only for healthcare and annuity payments, but also for education, investment projects or philanthropy. A trust fund is also established in an effort to preserve property and distribute it among blood relatives in such a way as to eliminate negative effects of a divorce or sudden death when property could easily fall outside the control of blood family. Last but not least, trust funds fulfill, in relation to descendants, a regulative function by a gradual releasing of money, thus preventing their uneconomical consumption.

A possible tax exemption of profit shares paid to trust funds is currently being discussed in the Parliament. The relevant law amendment was originally expected to come into effect on 1 April 2017; however, the Senate has referred the law amendment back to the Chamber of Deputies with several amendments, and the effective date will apparently be postponed to 1 May 2017 at the earliest (the effective date is set to be the first day of the calendar month following the publication date of the law amendment in the Collection of Laws).

The law amendment extends the current legislation applicable to capital companies and cooperatives. This means that if a trust fund holds at least a ten-percent share in the registered capital of a foreign subsidiary, a profit share payment to the trust fund shall be exempt from Czech withholding tax, or in the case of a foreign subsidiary, such a profit share payment shall not be included in the Czech tax base.

This will eliminate quite a significant tax barrier, which has put trust funds at a disadvantage so far.

Transaction and property monitoring – a beneficial owner, proving the origin of property, and electronic registration of revenues

Since the 1990s, there has been a growing tendency to make anti-money laundering and also counter-terrorism financing measures (so-called AML and CTF rules) stricter. As part of such measures, the EU Member States have an important obligation to implement, besides other instruments, the extension and a more detailed definition of a beneficial owner of a legal person, i.e. of a company and of an entity falling beyond the scope of the Companies Act, in their national laws. This area had been regulated in the previous AML Act of 1996, and such obligations have been significantly extended in the current AML Act No. 253/2008 Sb., in which the EU Directive No. 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing has been implemented, with effect from 1 January 2017, by an extensive law amendment (Act No. 368/2016 Sb.).
The amended AML Act includes extensive duties of obliged persons in the area of compliance and, in particular, in taking actions towards their clients leading to the identification and check of the clients, which are part of a due diligence procedure. Within the meaning of the AML Act, such a procedure leads to the identification of an acting person and, in particular, the determination of the purpose of a transaction, the economic reasons, and the financing sources of the relevant transaction. Beneficial owners shall be identified by the obliged persons, such as financial institutions of different types, attorneys-at-law, notaries, several other entities in the area of property management, real estate agents, and traders in other specified commodities.

The AML Act defines a beneficial owner as a natural person or persons who beneficially own or control a client, or on whose behalf a transaction or activity is carried out. A beneficial owner always is a natural person, including a statutory body, of a person holding a share in a client or voting rights corresponding to more than 25 percent. Beneficial owners may also include founders, fund recipients, including beneficiaries, trustees, and similar persons in relation to persons acting in accord or controlling persons.

Registration in the register of beneficial owners

The definition of beneficial owners will be significant in practice, particularly after 1 January 2018, when the regulation of registration in the register of beneficial owners, as part of the Act on Public Registers of Legal and Natural Persons, will come into effect. This will entail the obligation of persons registered in the Commercial Register to also register their beneficial owners in the non-public part of the Register. It must be noted that, for example, in the United Kingdom, the beneficial ownership register is publicly accessible.

In many cases, beneficial owners are persons who at the same time receive income from their controlled or otherwise related persons, and pay income tax therefrom. The Financial Administration, which will have access to the data of the beneficial owners of legal persons from 1 January 2018, is thus expected to use such information as part of its searching activities.

For practical reasons, legal persons are advised to identify and register their beneficial owners in the register in order to fulfil the registration obligation within a specified time period from the effective date of the amended AML Act (one year or three years, depending on the type of entity).

Electronic registration of sales

The second tool introduced as a tool to monitor property transactions by the State is electronic registration of sales (ERS or EET in Czech). Sales that are not carried out via wire transfer or deposit into an account must be registered in the eponymous system under Act No. 112/2016 Sb. on Registration of Sales. The ERS shall not apply to sales carried out via wire transfers. Sales must be registered by personal income tax payers and corporate income tax payers, whereas from 1 December 2016 sales must also be registered by accommodation and hospitality service providers, and from 1 March 2017 by retailers and wholesale-salers. Other entities, including liberal professions, and entities active in the agriculture sector or providing transportation services must register their sales from 1 March 2018. The exceptions are some crafts and production activities to be involved from 1 June 2018. A receipt that has been registered in an online regime, carries the FIK code (fiscal identification code), which is allocated to each receipt, and the BKP code (taxpayer security code) allocated to a specific taxpayer, i.e. a specific entity. Transactions are stored via the ERS in the central data storage, and the Financial Administration may analyse and search for non-standard transactions or methods of doing business by comparing them with other reporting tools.

Proving the origin of property

Another novelty in the legislation, which is, despite being inspired by foreign legislations, an original concept for Czech legislation, is proving the origin of property which has been supplemented to the Income Tax Act by an amendment thereto – Act No. 321/2016 Sb., amending certain acts in respect of proving the origin of property. Proving the origin of property, effective from 1 December 2016, originates from a previous idea to introduce property statements, that had, however, never been approved in the Czech Republic. It must be noted that proving the origin of property is focused on specific persons more than any other forms of property statements. Its aim is to enable personal income tax and corporate income tax administrators (i.e. first-instance financial authorities) to deliver to a taxpayer a request to prove his income under Section 38x of the Income Tax Act. They may do so as long as they reasonably consider that the taxpayer’s income that has been notified or reported to them does not correspond with an increase in his capital, consumption or other expenditure, and differs from the increase by more than CZK 5,000,000. Upon request, the taxpayer must prove the facts stated in
the request. If the taxpayer fails to prove the origin of his income, a tax administrator may, with respect to income that would be assessed with tax exceeding CZK 2,000,000, assess the tax using aids, and, at the same time, impose a special penalty of 50%, or 100% on the taxpayer if he fails to cooperate. If the amount of the increase in property is at least CZK 10,000,000, the tax administrator shall request that the taxpayer submits a declaration of property relating to all property except for movables and debts, both up to the value of CZK 100,000.

The aforementioned legal instruments entail specific compliance requirements. In order to fulfil the obligations ensuing from these two instruments practically, one must consider their existence by the time they become effective as a part of internal rules in an individual organisation. With respect to regulated entities, the form of such instruments may be reviewed by a supervision authority. Accordingly, paying a great deal of attention to their correct formulation and to the inclusion of all substantive rules in their wording is recommended, in order to eliminate a risk of possible secondary liability of your business for breaching the obligations by third parties which may occur.

New rules against tax avoidance in the internal market – ATAD Directive

In June 2016, the EU Council Directive 2016/1164, laying down rules against tax avoidance practices, has been adopted. These rules relate to corporate income tax within the internal market of the European Union. The Czech Republic must implement this Directive in its national law by 31 December 2018. The Directive follows from the BEPS project (Base Erosion and Profit Shifting) created within the OECD.

The Directive has an impact primarily on tax optimisation used by companies in the internal market, i.e. between the EU Member States. However, it also contains such rules that will affect tax accounting in corporate structures active only in a national market. It will mainly affect not only the use of debt instruments and external financing, such as bonds or leasing, but also profit payments to parent companies and other transactions between group members. There will be (or may be) a number of exceptions from, or certain mitigations in, rules under the Directive, all depending on what approach the Czech legislator will take with regard to that area.

Currently (until 30 April 2017), a public consultation is being held, under the responsibility of the Ministry of Finance, as to how this Directive will be reflected specifically in the Income Tax Act. It is established at a minimum protection level, so individual Member States must use at least the regime stipulated in the Directive, but they may also opt for a stricter alternative beyond the scope of the Directive (as shown in the following example of tax deductibility limitation). In our opinion, it will be necessary to anticipate the effects of the new legislation and to slowly adjust the approach to debt financing within corporate structures.

Limitation of interest expense tax deductibility

As part of the ATAD Directive, a rule on the limitation of interest expense tax deductibility for a tax period only up to 30% of EBITDA (i.e., earnings before interest, tax and depreciation) should be implemented. This limit is currently anticipated, but under the ATAD Directive, the Czech Republic may also set a lower limit. For now, it is not completely clear whether this rule will fully replace the current limitation of so-called “thin capitalization”, i.e. tax deductibility of interest on related party loans/borrowings where a ratio of principals of such loans to equity does not exceed 4:1, and with bank loans/borrowings to equity when such a ratio does not exceed 6:1 (for the sake of simplicity, hereinafter referred to only as the "loans").

A smaller part of current tax deductible costs will continue to be viewed as tax deductible under the new regime – with each transaction, one will have to consider the impossibility to deduct costs in the amount of the item "non-deductible exceeding borrowing costs," and thus a relative increase in tax liability with regard to a turnover with respect to certain companies. According to the OECD report, this rule will affect approximately 13% of companies in the EU.
The impact of this change may be simply shown in the following example. To simplify it, we assume that a company does not apply any depreciation, does not have any interest income, and (for the time being) does not pay taxes (of course, these items would otherwise increase EBITDA).

According to the current thin capitalization rules, interest expenses would be fully deductible for the tax period 2019 because:

- A ratio of principals of loans provided from related parties to equity does not exceed 4:1 (as they are 4000 : 1000; according to the applicable methodology, for the calculation purposes, the equity does not include profit or loss of the current period); and
- Principals of loans provided from non-related parties are not subject to any limitation.

However, according to the new rules, the interest for the tax period 2019 will be fully non-deductible because:

- Limitations will also apply to loans provided from non-related parties; and
- In our example, EBITDA is 0 (a loss of 500 is reduced by interest expenses of 500), i.e. the deductibility rule of up to 30% of EBITDA will make interest deduction completely impossible.

### Company’s balance sheet as at 31 Dec 2019 (in CZK millions)

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<th>ASSETS</th>
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<td>TOTAL</td>
<td>5500</td>
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Interest expenses 500 (10%, i.e., 400 + 100)

### Authors:

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- **Libor Kyncl** | Lawyer

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Havel, Holásek & Partners’ Private and International Client Practice Group joined by tax law specialist Josef Žaloudek

Havel, Holásek & Partners has been joined by senior associate Josef Žaloudek. An experienced lawyer specialising in corporate tax law and international taxation has further strengthened a team advising private clients. “We have developed legal and tax advice for the most prominent and affluent clients that include owners of successful Czech and foreign businesses, top managers, as well as freelancers or sportspeople since 2008. We currently have the largest team with such a specialisation in the market, and Josef Žaloudek is no doubt a great asset, mainly to the corporate component. He will be responsible primarily for direct taxation,” says the law firm’s managing partner, Jaroslav Havel. Josef Žaloudek started his career at the Czech Republic’s Ministry of Finance, where he spent almost four years. Before joining us, he worked for Deloitte Advisory and Ambruz & Dark Deloitte Legal for eight years, mainly focusing on international taxation, restructuring and related aspects of civil and commercial law.
Ascertaining a beneficial owner (not only) in tender procedures

On 1 January 2017, a new act no. 368/2016 Sb. amending act no. 253/2008 Sb., on certain measures against money-laundering and the financing of terrorism, as amended (the “AML Act”), entered into effect. This amendment provides a more precise definition of “beneficial owner”, and from 1 January 2018 it establishes a register of information on beneficial owners of legal entities to be kept at a registry court. At the same time, this amendment is the first more significant amendment of act no. 134/2016 Sb., on public procurement, as amended (the “Public Procurement Act”).

It is relevant in relation to public procurement that pursuant to the provisions of Section 104(2) of the Public Procurement Act, prior to awarding a contract, contracting entities must always require the selected contractor – a legal entity – to submit proof of the beneficial owner under the AML Act, and support the information with the relevant documents certifying how the beneficial owner is related to the contractor. Thus, under the amendment of the AML, depending on the date at which the beneficial owner is to be proven, from 1 January 2017, a different procedure will be applied than before 31 December 2016 as a consequence of a change in the definition of a beneficial owner, and subsequently, from 1 January 2018 the procedure will be further changed with regard to the new register which will already be in effect at that time.

From 1 January 2018, two new provisions will be inserted in the Public Procurement Act (Section 122(4) and (5) in place of the current provision of Section 104(2) of the Public Procurement Act. In accordance with these provisions, contracting entities will ascertain information about the beneficial owner of the contractor’s legal entity from the registry of beneficial owners under the law on public registers, and they will state such information in documentation relating to the public contract. Only if the contracting entity is not able to ascertain the contractor’s beneficial owner in this manner, it will then request the contractor to submit an extract from a register similar to the register of beneficial owners, or to provide identification details of all persons being the contractor’s beneficial owners, and to produce the relevant documents.

Under the amended AML Act, a beneficial owner is an individual actually or legally capable of directly or indirectly exercising a decisive influence in a legal entity, in a trust or other legal structure without a legal personality; provided that these conditions are met, the following persons are considered to be a beneficial owner:

a) in the case of a company, an individual

1. who alone or jointly with persons acting in concert with him holds more than 25% of voting rights of such a company, or has a share in the registered capital exceeding 25%,
2. who alone or jointly with other persons acting in concert with that individual controls the person specified under point 1,
3. is to be the recipient of at least 25% of the company’s profit, or
4. is a member of the statutory body, representative of a legal entity in such a body or in a position similar to the position of a member of a statutory body, if there is no beneficial owner, or if the beneficial owner cannot be ascertained in accordance with points 1 to 3,

b) in the case of an association, benevolent society, association of unit owners, church, religious society or other legal entity under the act regulating the status of churches and religious societies, an individual

1. who holds more than 25% of its voting rights,
2. who is the recipient of at least 25% of the funds distributed, or
3. who is a member of a statutory body, representative of a legal entity in such a body or who holds a position similar to the position of a member of a statutory body, if there is no beneficial owner, or if the beneficial owner cannot be ascertained in accordance with points 1 or 2,

c) in the case of a foundation, institute, trust, or other legal structure without a legal personality, an individual or a beneficial owner of a legal entity being in the position of

1. a founder,
2. a trustee,
3. a beneficiary,
4. a person in whose interest a foundation, institute, endowment fund, trust or other structure without a legal personality, if no beneficiary is determined, has been established or operates and
5. persons authorised to supervise the management of a foundation, institute, endowment fund, trust or other legal structure without a legal personality.

In practice, until 31 December 2017, contracting entities will be obliged to set out in tender conditions (except for a simplified below-the-limit procedure) the requirement that beneficial owners of a contractor – legal entity – be identified and that the relevant documents be submitted with the choice of the documents proving the relationship of a person designated by the contractor as the beneficial owner being left up to the contractor. After choosing a particular contractor, the contracting entity
will be always obliged (even in the case of a simplified under-the-limit procedure) to request the submission of an affidavit with the identification of beneficial owners, and the submission of the relevant documents (Section 122(3)(c) of the Public Procurement Act). The submission of information and documents concerning the beneficial owner is described more precisely in the methodology of the Ministry of Regional Development.

In contrast, a legal entity’s contractor will be obliged to disclose its ownership structure up to the level of individuals complying some of the definitions of a beneficial owner while it is not excluded for a legal entity to have several beneficial owners. For example, with more complex legal structures, where a legal entity has several subsidiaries, it will be necessary to assess each of them for the existence of individuals possessing the characteristics of a beneficial owner under the AML Act and to state each such individual in an affidavit along with such individual’s identification details (name and surname) and how they are related to the legal entity. It is also necessary to prove such a relationship with an appropriate document, such as an extract from the Commercial Register or other similar register, a list of shareholders, a statutory body’s decision on the payment of a share in profit, or a memorandum of association, founder’s deed or articles of association, as demonstrably listed in the Public Procurement Act. However, the relationship of the beneficial owner to a legal entity may also be proven with other documents such as an extract from a securities issue, an agreement on a joint concerted action, a brokerage agreement or any other agreement etc.

In the case of legal entities specified under letters a) and b) above, if there is no beneficial owner or if no beneficial owner can be determined to be a member of a statutory body, a representative of the legal entity in such a body or in a position similar to the position of a member of the statutory body of such a legal entity will be regarded as the beneficial owner, even if the relevant legal entity is controlled by one or more controlling legal entities. In this case the Czech legislation applies a procedure different from Slovak act no. 343/2015 Z. z. on public procurement, which provides under Section 11(3) that if there is no beneficial owner, all members of the legal entity’s statutory body who participate in the business, control or management of the given legal entity (i.e. members of the parent company’s statutory body) are regarded to be the beneficial owners. An explanatory opinion of the Slovak Public Procurement Office specifies that if a legal entity has several controlling persons, it suffices if members of the statutory body of the parent company exercising decisive influence in the subsidiary is identified as the beneficial owners.

After 1 January 2018, every legal entity will be obliged to file an application for registration of information about the beneficial owner in the registry of beneficial owners, including the name and address of the place of residence or domicile, as appropriate, if different from the place of residence, a birth date and birth certificate number, if assigned, nationality and information about (i) the share in voting rights, if the position of a beneficial owner is based in voting rights, if the position of a beneficial owner is based on a direct participation in the legal entity, (ii) the share in distributed funds if the position of the beneficial owner is based on the beneficial owner being the recipient of the distributed funds, or (iii) other facts, if the position of the beneficial owner is constituted differently.

Legal entities will also be obliged to keep and record, on a continuous basis, up-to-date data for the purposes of ascertaining and verifying the identity of their beneficial owners including information relating to fact which constitutes the position of a beneficial owner and to keep such records and information for the entire period during which the person will be the beneficial owner, at least 10 years from the cessation of such a relationship.

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On 14 January 2017, an amendment to Act No. 90/2012 Sb. on Companies and Cooperatives (the “CA”) (the “amendment”) came into effect. The amendment has reintroduced into Czech law the right of employees to be involved in the functioning of a joint stock company, specifically through the right to elect and recall a corresponding share of the joint stock company’s supervisory board members, if the joint stock company employs more than 500 employees in an employment relationship.

Employee involvement in a joint stock company’s supervisory board is nothing new in the context of Czech law. Similar legislation, inspired by the German-Austrian model of the two-tier system of a joint stock company’s bodies, had been in force in Czech law until 2013, and had been revoked in connection with the private law recodification as at 1 January 2014. Considering that in this respect, the recodification was not completely compliant with EU law and modern legislation which favours employee involvement in the functioning of companies, the legislator has decided to restore, to a certain extent, the previous legislation. The reason for reintroducing employee involvement in the functioning of a joint stock company is also the fact that until 2013, many joint stock companies had considered employee involvement as functional and desirable, but the new legislation had basically also made employee involvement impossible for the companies that would like to continue in established practice.

From the proposed changes, only a small fraction was incorporated in the approved wording of the amendment. The resulting wording of the amendment reintroduces the obligations concerning a joint stock company’s supervisory board into the legal regulation of a joint stock company very ambiguously, and it is a legal regulation that is in by no means complete. The main problem is that one cannot give a clear answer to the question of whether the new legal regulation should also apply to joint stock companies having a so-called “one-tier” structure of corporate bodies (a statutory director instead of a board of directors and an administrative board instead of a supervisory board). Although the CA stipulates that the provisions regarding the supervisory board may be applied to the administrative board accordingly, the supervisory board and the administrative board are not exactly the same bodies as regards their nature. By a different interpretation of the relevant provisions of the CA, one can come to both positive and negative answers. As a more comprehensive regulation which would address this issue unambiguously was deleted from the amendment and was not approved during the legislative process, it only remains to be seen how theory and case law will address this issue.

In line with the transitional provision of the amendment, all joint stock companies having more than 500 employees in an employment relationship will have to adapt their articles of association and the composition of their supervisory boards to the new wording of Section 448 of the CA in a way that the number of the supervisory board members must be divisible by three, and the composition of the supervisory board must be brought in line with the law within two years from the effective date of the amendment (i.e. by 14 January 2019). If a joint stock company fails to meet the statutory requirements, this may result, in extreme cases, in its liquidation.

The two-year period for implementing the required changes seems to be a sufficient period for taking all necessary steps. However, please note that joint stock companies having a higher number of employees, or a complicated or foreign ownership structure, should not wait too long in preparation for the required changes. As a matter of fact, one must take into account the steps which most of the affected joint stock companies will have to take and the necessary time sequence (convocation and holding of a general meeting in attendance of a notary public, election of the supervisory board members by employees, and registration of changes in the Commercial Register).

Aside from the possibility of fulfilling the above obligation, one can, of course, consider alternative solutions (division of a joint stock company into functional units, a change of a legal form, etc.), which it would be appropriate to select with regard to a specific situation of a given joint stock company.

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Occupational medical service in a new shape

The year 2017 marks many changes in the area of employment law. Apart from prepared amendments to the Labour Code, the Act on Residence of Aliens and the Employment Act, legislative changes will also significantly affect occupational medical services. Specifically, an amendment to Act No. 373/2011 Sb. on Specific Health Services, as amended (the “SHS Act”) and to related Decree No. 79/2013 Sb., implementing certain provisions of Act No. 373/2011 Sb. on Specific Health Services, as amended (the “OMS Decree”).

It is not yet apparent when exactly this amendment will come into effect. Originally, it was intended to come into effect on 1 January 2017; however, the amendment is still being discussed in the Chamber of Deputies. Despite this, we would like to inform you of the most important changes, as we believe they may be useful for your professional life.

The major proposed innovation is determination of a moment when an employer must have available a medical assessment of a job applicant from an occupational medical service provider. For the sake of clarity, this refers to the provider with whom the employer has concluded a written agreement in accordance with the SHS Act (the “OMS Provider”). Under the existing legislation, an employer must obtain such an assessment before concluding an employment agreement. This is very impractical in situations where the parties wish to agree in advance on conclusion of employment, but they do not want to negotiate about a future employment agreement. But in fact, the absence of a medical assessment prior to such a date results in a void employment agreement, which, in practice, many employers do not realise.

Under the new legislation, such an obligation should be stipulated prior to the establishment of employment, i.e. de facto not later than the day prior to the date of commencement of work by the job applicant.

A similarly important change is shortening the intervals of medical examinations of employees performing working activities in the second category (from 5 years to 4 years for employees aged under 50, or from 3 years to 2 years for employees aged over 50), and a change of the intervals of medical examinations of employees working at night (from one year to two years). Under the transitional provisions of the OMS Decree, the validity of existing medical assessments should not be affected by the amendment.

Employers will be obliged to send an employee to a medical examination in shortened intervals only after the expiry of validity of existing medical assessments, unless same cease to be valid on other statutory grounds.

Also, the amendment will introduce the definition of a “long-term loss of medical fitness”, which means such an unfavourable health condition of an employee which excludes him/her from undertaking existing work for a period longer than 180 days. This period is based on how a long-term loss of medical fitness is perceived from a medical perspective and is significantly shorter than the period applied so far based on the existing case law of the Czech Supreme Court, according to which this must relate to an exclusion from a working process for a period of at least one year.

The amendment will also introduce a new obligation of employers to send an employee to an extraordinary medical examination based on the OMS Provider’s instructions or the right of job agencies to demand that their employees (job applicants) pass a medical examination at user employers’ OMS Providers. Naturally, the costs will primarily be covered by job agencies. However, it would be appropriate to bear this in mind when concluding temporary job assignment agreements with job agencies.

The amendments to the SHS Act and to the OMS Decree will entail much more changes than we can discuss in this article. Accordingly, it would be appropriate to become familiar with these new changes sooner rather than later, e.g. at some of our specialised seminars in the spring of 2017, and to be sufficiently prepared for their introduction into practice.

Authors:
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Veronika Plešková | Senior Associate

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1 This article has been written based on draft amendments to the legal regulations concerned, as amended as at 27 January 2017.
2 Only in exceptional cases an assessment from the OMS Provider may be replaced with an assessment issued by a job applicant’s registering medical doctor.
Undoubtedly, developers (investors) are the most important parties when it comes to construction projects. Developers finance the construction, coordinate every step, and are responsible for the results. However, the moment there are any objections or actions filed in relation to a zoning decision or building permit, developers are forced to “play second fiddle”.

Developers may find out about any disagreement on the side of neighbours, environmental groups, or local authorities (referred to as complainants) relating to a construction project from the filed objections in first-instance construction or zoning proceedings. The building authority must address these objections in its decision, against which complainants can file appeals. When an appeal is filed, it is a warning that the complainants may challenge actions and appellate decisions if their appeals were to be rejected. How should a developer proceed if an enforceable appellate decision has been issued and the decision is likely to be challenged?

If a certain complainant files a petition against an appellate decision on the zoning decision or the building permit, only the complainant and the appellate building authority will be parties to the proceedings in accordance with the Code of Administrative Procedure. This is a rather unique situation. The developer requested the issuance of the decision, and the decision-making burden lay with the first-instance building authority. However, the parties to the court proceedings will be completely different entities. Under the Code of Administrative Procedure, the developer will only be in the position of a “person participating in the proceedings”, which is weaker from a procedural standpoint. In addition, even this status is not automatically acknowledged.

In practice, the developer might not even know that a petition was filed against the zoning decision or its building permit, or that a lawsuit has been filed or that court proceedings are taking place. It is very often the case that the developer finds out about the proceedings after an unfavourable judgement has been issued. Thus, the developer must monitor the situation at the relevant court after the enforceable appellate decision has been issued for the entire period that a complainant could file a petition. The deadline for filing petitions is two months after the claimant was notified of the decision in writing or by another method set out under law.

The developer should then file a request for it to be treated as a person participating in the proceedings. This request must provide a detailed justification. After that, the developer could, for example, react to the action itself or to the statements of other persons participating in the proceedings in order to attain the suspensory effect of the action. This is important, because if the court acknowledges the suspensory effect, for example, relating to an action against the enforceable building permit, the building permit would no longer be enforceable until the final decision has been adjudicated. However, court proceedings could last several months. So the developer would not be able to continue with construction for the entire period, even if construction has already begun.

The developer will also be able to participate in the court proceedings, inspect materials in the file, and request that it be given the opportunity to speak in court. The developer may also file an appeal in cassation at the Supreme Administrative Court, provided that the administrative court decided against the developer.

On the other hand, the “subordinate” position of a developer as only a person participating in the proceedings is reflected in the fact that the court could reject its request for a hearing altogether. If a hearing is held, the court would place the developer’s representative among the public, and not at the bench on its right or left hand as the claimant and the representative of the building appeals authority. The final word would be given to the claimant, and the building appeals authority, and the developer would need to present its arguments to the court before them. In addition, the chance of recovering the costs of the proceedings for the developer (in particular, legal representation) when upon succeeding in the proceedings would be very slim.
In December 2014, Directive 2014/104/EU took effect governing certain issues related to damages for anti-competitive behaviour by cartels and abuse of dominant position. The objective of the directive is, in particular, to alleviate the position of the injured parties before the court, as well as to protect businesses providing efficient cooperation in exposing cartels. The directive was to be implemented by 27 December 2016. In neighbouring countries, an implementation law was only adopted in Slovakia on 29 November 2016. In Germany and Austria, as well as in the Czech Republic, an implementation bill is currently undergoing a more or less advanced stage in the Parliament.

Unlike Austria and Germany, the Czech and the Slovak legislature have decided to implement the directive by means of a separate act rather than by amending existing acts.

Given that the implementation period has expired, the bill was presented to the Chamber of Deputies with a proposal for adoption in a first reading. However, it is not clear when it will be discussed, and whether it will indeed be adopted in the first reading.

As the directive governs horizontal relationships between individuals and not vertical relationships to the state, the direct effect of the directive cannot be invoked after the expiry of the implementation period.

What the new act is expected to bring

The directive and hence the implementation act will bring new rules affecting substantive aspects of liability, as well as procedural rules for exercising claims to damages. The changes will primarily apply to:

- the scope of damages (besides actual damage and loss of profit, the injured party may also claim compensatory interest reflecting the effluxion of time);
- the length and running of the limitation period and joint liability of a cartel members;
- the alleviation of the injured party’s position in terms of evidence by means of rebuttable assumptions and rules applicable to discovery; the bill even contains a variation of the US pre-trial discovery by introducing a possibility for the injured party to file a request with the court to disclose specific categories of evidence before the proceedings for damages are initiated.

Protection for leniency applicants

Besides alleviating the position of the injured party, an equally essential aim of the legislature was protecting one of the most important tools for exposing and prosecuting cartels by competition authorities – the leniency programme (i.e. immunity from penalties or reductions in penalties in exchange for reporting or providing evidence of a cartel).

A successful applicant for leniency who was granted immunity from the penalty and did not lodge an appeal against the decision of the competition authority should be protected in particular from becoming the focus of concentrated interest from all injured parties, and could only be sued by its direct and indirect customers and suppliers.

Also, applications for leniency and related statements of the applicant as well as evidence provided through the leniency should also be protected against use as evidence in damages litigation.

Authors:
Robert Neruda | Partner
Petra Joanna Pipklová | Legal Expert

Havel, Holásek & Partners receives the highest rating for competition law in the Czech Republic from the prestigious British agency Global Competition Review

Our office has been included in the prestigious competition law yearbook, GCR 100, published by the United Kingdom’s Global Competition Review (GCR). In the 17th Edition of the publication which sums up achievements in 2016, our firm is among leaders of competition law and economics in the Czech Republic with the highest possible rating of Elite, and among highly recommended advisors in the same practice areas in Slovakia (rating of Highly Recommended).
An amendment to the Employment Act will affect agency employment and employing disabled persons

The Czech Parliament’s Chamber of Deputies is currently discussing a draft amendment to the Employment Act. In practice, the amendment can bring a number of changes, having a major impact on both employers and employees. The amendment has gone through a second reading stage in the Chamber of Deputies and, if adopted, the changes will become effective during 2017. The most important modifications are summarised below.

Job agencies

Major changes will affect agency employment. Under the new rules, applicants for an employment agency licence will be required to make a security deposit of CZK 500,000 with the Directorate General of the Employment Authority. This obligation will also apply to existing job agencies, which will be required to make the deposit within 3 months of the effective date of the amendment. The objective of this measure is to prove the employment agency’s financial capacity, to ensure its successful existence, and to eliminate employment agencies established for questionable purposes.

The amendment also defines requirements for the execution of the office of an agency’s representative in charge. The representative will be required to perform his/her activity in employment with agreed working hours of at least 20 hours per week. This requirement will not apply to those representatives in charge who are concurrently part of the employment agency’s executive body.

The employment agency licence will be issued for a period of 3 years, which is the same period as now. However, if an extension is applied for, the licence may be granted for an indefinite period.

The amended Employment Act will stipulate other reasons for which an employment agency licence can be revoked. These include inactivity (no employee assigned with the user for a period of 2 years), or a failure to provide a certificate of bankruptcy insurance.

Alternative performance for employing disabled persons

If adopted as proposed, the amendment will change rules governing compliance with the mandatory share of disabled employees. This requirement may be alternatively complied with by means of purchase of goods or services. Employers will only be allowed to provide such products or services as alternative performance if they enter information about the performance in a register, which will be kept by the Ministry of Labour and Social Affairs, within 30 days of the payment for the performance.

Other changes

The amendment will introduce other changes, such as extending the maximum period of providing benefits for a socially beneficial employment position, increasing employee privacy protection, regulations governing ‘non-colliding’ employment of work-seekers, or more precise rules applicable to the disclosure of data about insolvent employers. Nevertheless, these are rather minor changes.

Author: Jan Koval | Partner

Havel, Holásek & Partners recognised as law firm with best work environment in the Czech Republic

Our office was recognised with an award in the first year of the Offices of the Year competition, which aims at awarding firms investing in quality work environment. A professional jury composed of leading experts in the field of architecture, design, office equipment and HR assessed office interiors in nine categories in terms of exceptionality and design, innovation, overall atmosphere, and, in the first place, quality of work environment for employees. We won first prize in the “law firms” category.
Morocco: a piece of the EU in Africa

Attributing Morocco with terms such as the “Gateway to Africa” is a tradition that goes back hundreds of years. However, it not only refers to the historical romanticism connected to caravans crossing the Sahara or its current popularity with tourists. Morocco also has something to offer exporters. We most likely will not find a country on the African continent closer to the European Union. It would not even be too much of an exaggeration to refer to it as an outpost.

“A place where everything takes a long time, but more or less functions. At least if you speak French.” We are talking about Morocco, but it’s not by chance that this could also refer to the Francophone countries of the EU. French is the most common business language in Morocco (though Spanish is also useful in the northern territories), but also the basis for its rule of law and legal reasoning, including typical literalism, i.e. adherence to the literal version of agreements, or the principle that agreements with government authorities and other public entities are of an “administrative” character and are under the jurisdiction of the administrative courts.

In addition, it is not only in Africa that we come across the most common complaint of entrepreneurs relating to payment morale. Nevertheless, Morocco is only one step ahead when it comes mandatory payment periods: for state institutions, a minimum of 90 days, for all others, a minimum of 60 days. In practice, it is even somewhat worse, so it is recommended to have quality security or to make payments through a letter of credit. On the other hand, Morocco is known for being a recipient of assistance from European funds, and this means the possibility of participating in projects that are also accessible to us.

In general, it is an open economy that has a high level of interdependence with Europe. Morocco is a country in the Euromed region. It has an association agreement with the EU and supplementary liberalisation agreements, e.g. in trading agricultural products (including an agreement on acknowledging the geographical designations of agricultural products). Customs barriers were eliminated in 2012 in the area of industrial products. In 2013, negotiations on a Deep and Comprehensive Free Trade Area (i.e. DCFTA) were launched and have yet to be completed. However, in relation to the Czech Republic, there is also an agreement on the promotion and protection of investments as well as a double taxation agreement. International investment arbitration is also possible in the ICSID system.

In the event of disputes, we recommend relying on local justice only to a limited degree. It is very time-consuming. International arbitration, though, is admissible, and its verdicts are usually properly enforced. Morocco also acknowledges foreign court decisions under the terms of reciprocity. However, we are not aware of any case law in relation to the Czech Republic.

**Author:**

**Martin Ráž | Senior Associate**

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Law school students consider Havel, Holásek & Partners the most sought-after employer in the Czech Republic

Our firm was named the most sought-after employer in the Czech Republic among law firms in the TOP Employers for the third year running. In addition, Havel, Holásek & Partners was also recognised by law school students with the best academic results as number one in the Lawyer category, which has been dominated by international law firms in previous years. The results of the study were published by the Association of Students and Graduates. “If there is something to be expected in the current legal market, then it is competition in hiring young, talented lawyers. We are pleased that we are seen by the coming generation of lawyers as a prestigious and attractive employer. We even received more preference votes from students with the best academic results than foreign law firms which had previously been the highest target to aim at for most students, even during my studies. I wish to thank to all students who took part in the survey, and I trust that we will start a successful collaboration with many of them,” says Jaroslav Havel, managing partner.
Changes in Slovak income tax

Effective from 1 January 2017, an amendment to the Slovak Income Tax Act came into effect. The amendment has entailed a number of major changes in taxation of legal entities and natural persons:

Reducing the corporate income tax rate

The amendment has reduced the corporate income tax rate from the original rate of 22% to 21% and the lower tax rate will apply for the first time to taxation period starting from 1 January 2017.

Taxation of dividends and liquidation surplus

The amendment has also introduced taxation of income from dividends paid out to natural persons as follows:

- dividends from profits recognised for the period until 31 December 2003 will be subject to a 7% withholding tax;
- dividends from profits recognised in the period from 1 January 2004 to 31 December 2016 will not be subject to tax;
- dividends from profits recognised in the period from 1 January 2017 will be subject to a 7% withholding tax.

The legislator has thus abandoned the original proposal of the Slovak Finance Ministry to tax dividends at the rate of 15%.

Dividends paid out to residents having limited tax liability (i.e., non-residents) will be considered as income originating from sources in the territory of the Slovak Republic and will be subject to withholding tax (which may be reduced if a double taxation treaty applies). The dividends which the Slovak companies pay out to residents of non-contractual states or which they receive from residents of non-contractual states will be subject to a 35% withholding tax.

Given (re)introduction of taxation of dividends, the dividends from profits after 1 January 2017 with respect to natural persons will not be subject to health insurance.

The amendment has also introduced, for example, taxation of a settlement share and of a liquidation surplus share. A liquidation surplus will be subject to tax if a company enters into liquidation as of 1 January 2017. In this case, a 7% withholding tax will be applied.

Income tax will not apply to an entrepreneur’s initial contribution (e.g., a monetary contribution at the establishment of a limited liability company). Yet prior to taxation, a liquidation surplus share will be reduced by that sum of the contribution, and tax will be calculated only from the resulting difference. Other expenses related to liquidation will not be tax deductible.

Cancellation of tax licences

The last period for which tax payers will be obliged to pay a tax licence (a so-called minimum corporate income tax) will be the year 2017, if their taxation period is identical to a calendar year. If a taxation period is identical with a fiscal year, taxpayers will last pay a tax licence for the taxation period ending in the course of 2018. Tax payers may offset a paid tax licence also after this period, subject to further statutory conditions.

Increasing flat-rate expenses of self-employed individuals

The limit of self-employed individuals’ flat-rate expenses has been increased from the current 40% to 60%, however, up to EUR 20,000 as a maximum per year. For comparison, by the end of last year, the maximum
amount of flat-rate expenses had been set at a fixed sum of EUR 420 per month (i.e., EUR 5,040 per year).

**Tax deductibility of certain expenses after their payment**

The amendment adjusts the existing provision conditioning tax deductibility of some costs after their payment. Since 2017, various licence fees, e.g., for granting the right of use or the right to use an object covered by industrial property rights, computer programs (software), know-how, etc., shall be tax deductible only after their payment.

**Changes in transfer pricing**

The amendment specifies the obligation to keep transfer pricing documentation by defining the term “controlled transaction”, replacing the term “mutual business relationship”. Another change is the setting of prices for approving a transfer pricing method. The previous fee, which represented one per cent of the volume of forecast transactions, is replaced with a fee set directly in the law, in the amount of EUR 10,000 for unilateral approval and EUR 30,000 for approval of applying a pricing method based on a double taxation treaty.

Another change brought about by the amendment includes stricter fines, as twice as much as existing ones, for deliberate avoidance and purposeful circumvention of tax liability in connection with incorrect price setting in controlled transactions. Said fines will be imposed if Tax Authorities learn the following circumstances based on tax inspection:

- a tax payer has incorrectly set the transfer prices and, based on this, it has reduced the tax base or increased the tax loss;
- the transfer prices have been set for the purpose of reducing a tax payer’s tax liability.

A certain form of effective repentance will be expressed when a tax administrator will not impose a double penalty in cases where a tax payer acknowledges his fault, and, at the same time, pays the difference of the tax assessed within a set period.

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**Author:**

David Neveselý | Partner

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**Havel, Holásek & Partners recognised as the best law firm in IT in the Czech Republic**

Our office has been recognised by Corporate INTL as the 2017 Law Firm of the Year in the Czech Republic in IT law. Havel, Holásek & Partners’ practice group specialising in information technology, as well as in telecommunications, media and intellectual property protection, is one of the largest in the Czech Republic and Slovakia. The law firm advises a number of leading companies in the IT market and investors expanding their portfolios by investing in technology firms. Legal advice is provided on issues such as software development and copyright protection, IT system integration projects, outsourcing agreements, distance selling contracts and electronic contracts, contracts between internet companies, data storage, use of content and liability for content on the internet, competition protection, or representation in disputes arising from complex IT related contracts and disputes in connection with domain names.
We support the education of managers

Also in this year, we carry on supporting the publishing of the best practically oriented international books for managers and firm owners. “We have selected the best of the management literature at various publishing houses which we have drawn on and by which we have been inspired over the years for the management of our own law firm. We believe that, in this way, we can contribute to the professional development of Czech managers and promote further cultivation of the local business environment”, says Jaroslav Havel. The recent “contribution” is the Czech translation of the foreign bestseller *Dilemmas of Family Wealth* by Judy Martel, a recognised expert in succession in family businesses. We’ve published the book under the title *Rodinné firmy na rozcestí* (in English: *Family Businesses on the Crossroads*), by which we want to evoke particularly the specific situation in the Czech Republic where generations in family businesses are replaced for the first time after the fall of the totalitarian regime. Foreign experience may, in this respect, serve as a good advisor.

In previous years, John Kotter’s *Leading Change*, *The Leadership Code* by Dave Ulrich, Norm Smallwood and Kate Sweetman, and *Good to Great* by Jim Collins have already been published. Last year, we supported the publishing of the first Czech edition of the bestseller *Built to Last* by Jim Collins and Jerry I. Porras, *Private Equity* by Orit Gadiesh and Hugh MacArthur, and *The Essentials – 10 articles from Harvard Business Review’s most influential authors.*

Support of pro bono projects

Also this year, we have leveraged the Lawyer of the Year event to publicly support projects we appreciate and stand behind. During the evening ceremony, our managing partner Jaroslav Havel presented two charity checks. The first, in the amount of CZK 100,000, was given to the foundation fund AutTalk. This fund helps parents manage care for their autistic children by direct financial support of such families or by free-of-charge social and legal, psychological or rehabilitation advice. The second, in the amount of CZK 50,000, lent our support to fund raising for the construction of a new organ in St. Vit Cathedral.

Havel, Holásek & Partners joined by Renáta Šínová, a top expert in Civil Procedure

Our office has strengthened its team with another leading expert. Renáta Šínová (38) of the Faculty of Law of Palacký University in Olomouc is a prominent specialist in Civil Procedure and family law. Working closely with Havel, Holásek & Partners as an Of Counsel, Renáta Šínová will primarily participate in the activities of the Havel, Holásek & Partners Academy, joining the largest academic team specialising in civil law in a single law firm operating in the Czech Republic.
The Havel, Holásek & Partners Academy is preparing for the summer semester these workshops among others:

**PRAGUE**

- **28 April**  Amendment to the Labour Code concerning managers
- **5 May**  Case law of high courts concerning pledge
- **12 May**  Case law of high courts concerning security of receivables
- **19 May**  Strategy in the conclusion of IT agreements, with a focus on the drafting and delivery stage
- **26 May**  Novelties regarding consumer protection
- **2 June**  Case law of high courts concerning unjust enrichment
- **9 June**  Revolution in personal data protection
- **16 June**  Penalties under the Act on Register of Contracts
- **22 June**  Reform of administrative enforcement law
- **23 June**  Legal aspects of autonomous vehicles, robots and drones

**BRNO**

- **19 May**  Amendment to the Labour Code concerning managers
- **23 June**  Revolution in personal data protection

Seminars are held in the modern offices of the Florentinum building in Prague on Fridays from 9 to 12:30. Our lecturers are leading experts, academics and co-authors of the new Civil Code and major commentaries on the Civil Code – Milan Hulmák, František Korbel, Filip Melzer, Renáta Šínová and Petr Tégl.

For more information, please visit: www.havelholasek.cz/akademie

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**Petr Tégl, Of Counsel with Havel, Holásek & Partners, appointed docent**

Petr Tégl, an Of Counsel at Havel, Holásek & Partners and one of the main lecturers at its Academy, successfully defended his habilitation thesis on Public Lists under the Civil Code at the Faculty of Law at Palacký University in Olomouc, and obtained his habilitation on 30 November 2016. He was appointed a docent for civil law with effect from 1 February 2017.
Our team

180 lawyers | 500 employees

Our clients

1,000 clients | 70 of the Fortune 500 global companies
50 companies in the Czech Top 100 league | 7 companies in the Czech Top 10 league

International approach

Legal advice
in more than 60 countries of the world
in 12 world languages
up to 70% of cases involve an international element

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