

Czech Republic publishes draft proposal on Mandatory Disclosure Rules

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Executive summary

In March 2019, the Czech Government published draft legislation (accompanied by explanatory notes) implementing the European Union (EU) Directive on the mandatory disclosure and exchange of cross-border tax arrangements (DAC 6 or the Directive).

The Czech draft legislation is subject to the formal legislative process and may be amended before final enactment. If implemented as currently proposed, the Czech Mandatory Disclosure Rules (MDR) legislation will be broadly aligned to the requirements of the Directive.

The draft law legislative approval process outline is not known at this point.

Detailed discussion

Background

The Council of the European Union Directive 2018/822 of 25 May 2018 amending Directive 2011/16/EU regarding the mandatory automatic exchange of information in the field of taxation (the Directive or DAC 6), entered into force on 25 June 2018.¹

The Directive requires intermediaries (including EU-based tax consultants, banks and lawyers) and in some situations, taxpayers, to report certain cross-border arrangements (reportable arrangements) to the relevant EU Member State tax authority. This disclosure regime applies to all taxes except value added tax (VAT), customs duties, excise duties and compulsory social security contributions.² Cross-border arrangements will be reportable if they contain certain features (known as hallmarks). The hallmarks cover a broad range of structures and transactions. For more background, see EY Global Tax Alert, [Council of the EU reaches an agreement on new mandatory transparency rules for intermediaries and taxpayers](#), dated 14 March 2018.

EU Member States are to adopt and publish national laws required to comply with the Directive by 31 December 2019. The Czech Republic will as a consequence introduce domestic legislation, which should take effect from 1 July 2020.

Scope of taxes covered

The scope of the taxes covered under the Czech draft legislation does not go beyond the scope of the Directive and thus generally applies to all taxes except VAT, customs duties, excise duties and compulsory social security contributions.

Reportable arrangements

Under the Directive, an arrangement is reportable if:

- ▶ The arrangement meets the definition of a cross-border arrangement.
- ▶ The arrangement meets at least one of the hallmarks A-E specified in Annex IV of the Directive.

Under DAC 6, cross-border arrangements are defined as arrangements concerning more than one Member State or a Member State and a third country. The hallmarks can be distinguished as hallmarks which are subject to the main benefit test (MBT), and those which by themselves trigger a reporting obligation without being subject to the MBT. The overall definition of reportable arrangements included in the draft Czech legislation aligns with the DAC 6 definition.

Hallmarks A-E of the Directive

Most elements of the hallmarks included in DAC 6 are not expressly defined. The Czech draft legislation and explanatory notes do not provide clarification on these elements.

Main benefit test

In accordance with DAC 6, the MBT will be satisfied if it can be established that the main benefit or one of the main benefits which, considering all relevant facts and circumstances, a person may reasonably expect to derive from an arrangement, the obtaining of a tax advantage.

The MBT included in the Czech draft legislation follows the same logic and structure.

A minor departure from DAC 6 noted in the draft Czech legislation is that the MBT is not required to be satisfied where hallmark C paragraph (b) (i) is triggered. This hallmark relates to an arrangement involving deductible cross-border payments between associated enterprises where no corporate tax or corporate tax at the rate of zero or almost zero is imposed. It is not clear whether this is an omission or an intention. This point may be amended in the later stages of the legislative process.

Intermediaries

Under the Directive, intermediaries with EU nexus have the primary obligation to report arrangements to the tax authority. The Directive gives Member States the option to exempt intermediaries from the obligation to report where the reporting obligation would breach legal professional privilege (LPP). If there are no intermediaries which can report, the obligation will shift to the taxpayers.

Czech draft law proposes an exemption from the MDR obligation for certified Czech tax advisers and attorneys based on LPP. The exemption from reporting will also apply to persons to whom the LPP exemptions are granted by other EU countries' laws implementing MDR. When the professional privilege exemption applies, the MDR obligation transfers to any other involved (not-exempt) intermediary or - if none exists - to the relevant taxpayer (assuming the exempt tax adviser/attorney notifies the other intermediary or the relevant taxpayer about this waiver and provides the necessary information).

Reporting deadlines

Under DAC 6, for intermediaries (and relevant taxpayers), the trigger events for reporting under the Directive (from 1 July 2020) are when the reportable arrangement is "made available for implementation"; or when the reportable arrangement is "ready for implementation" or when "the first step of implementation has been made."

Under the Directive, reporting starts from 1 July 2020 and exchanges between jurisdictions from 31 October 2020. However, reports will retroactively cover arrangements where the first step is implemented between 25 June 2018 and 1 July 2020.

The Czech reporting deadlines are aligned with DAC 6.

Penalties

Penalties for failures to report (or failures to provide information concerning the LPP exemption) up to a maximum of CZK1.5 million (approx. €60k) are proposed to apply.

Next steps

The legislative approval process outline for the draft legislation is not known at this time. The Czech draft legislation and explanatory notes do not provide much clarification on the implementation detail and it is unknown whether the Czech Ministry of Finance will issue more detailed guidance addressing further implementation detail and examples.

Determining if there is a reportable cross-border arrangement raises complex technical and procedural issues for taxpayers and intermediaries. Taxpayers and intermediaries who have operations in the Czech Republic should review their policies and strategies for recording and reporting tax arrangements so that they are fully prepared for meeting their obligations.

Endnotes

1. For background on MDR, see EY Global Tax Alert, [EU publishes Directive on new mandatory transparency rules for intermediaries and taxpayers](#), dated 5 June 2018.
2. DAC 6 sets out a minimum standard. Member States can take further measures; for example, (i) introduce reporting obligations for purely domestic arrangements; (ii) extend the scope of taxes covered; (iii) bring forward the start date for reporting.

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EYG no. 001876-19Gbl

1508-1600216 NY
ED None

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