

Doing Business in the Czech Republic

2008



Contents

1. Introduction.....	1
2. Business environment.....	2
3. Foreign investment.....	8
4. Setting up a Business.....	13
5. Labour	17
6. Taxation.....	28
7. Accounting & reporting.....	48
8. UHY firms in the Czech Republic	50
9. UHY offices worldwide	50

1. Introduction

UHY is an international organisation providing accountancy, business management and consultancy services through financial business centres in over 70 countries throughout the world. Business partners work together through the network to conduct trans-national operations for clients as well as offering specialist knowledge and experience within their own national borders. Global specialists in various industry and market sectors are also available for consultation.

This publication is current at September 2008.

Every effort has been made to ensure that the facts in this booklet are correct at the time of going to press. However, no responsibility for loss incurred by any person acting or refraining from acting as a result of any material in this publication can be accepted.

This detailed report providing key issues and information for investors considering business operations in the Czech Republic has been provided by the office of UHY representatives:

AUDITOR, spol. s r. o.
Haštalská 6
110 00 Praha 1
Czech Republic
Email: praha@auditor-eu.com
Website: www.auditor-eu.com

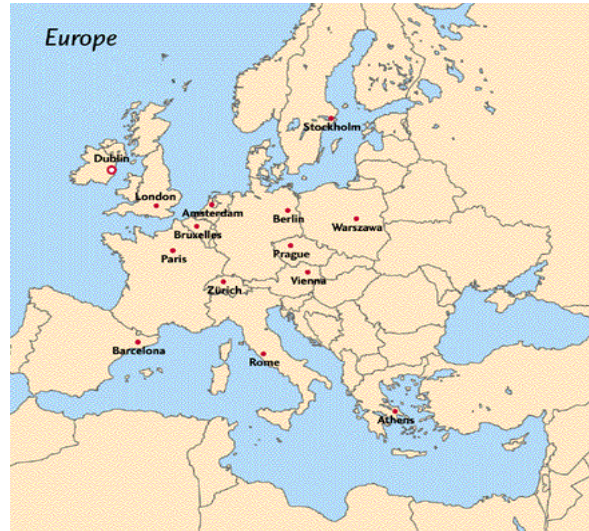
You are invited to contact Georg Stöger, managing partner, with any further inquiries you may have.

We look forward to helping you to do business in the Czech Republic.

AUDITOR, spol. s r. o. is a member of UHY, an international association of independent accounting and consultancy firms, whose organizing body is Urbach Hacker Young International Limited, a UK company. Each member of UHY is a separate and independent firm. Services described herein are provided by AUDITOR, spol. s r. o. and not by Urbach Hacker Young International Limited or any other member of UHY. Neither Urbach Hacker Young International Limited nor any member of UHY has any liability for services provided by other members.

2. Business environment

Geography



Location: centre of Europe.

Total area: 78,864 sq km

Neighbouring countries: Slovak Republic, Austria, Poland, Germany.

Main regions: Bohemia, Moravia.

Regional segmentation: lowlands, highlands, mountains – along the state borders.

Climate: mild continental.

Population: 10.2 million.

Population density: 131 inhabitants/sq km.

Ethnic groups: Czech (94%), Slovak (3%), Romany (1.5%), Polish (0.6%), German (0.5%), other (0.4%).

Religions: Roman Catholic (26,8%), atheists and citizens without religious affiliation (59.0%), other (14.2%).

Average life expectancy: men – 73.4 years, women – 79.7 years.

Urbanisation: More than 70% of the population lives in urban areas.

Further information

State: established as a parliamentary republic with a bicameral parliament (Chamber of Deputies and Senate).

State system: plural democracy.

Capital city: Prague (population: 1.2 million).

Official language: Czech.

Currency: Czech crown (CZK) = 100 halers.

Membership of international organisations: UN, NATO, WTO, Council of Europe, OECD, UNESCO, UNICEF, WHO.

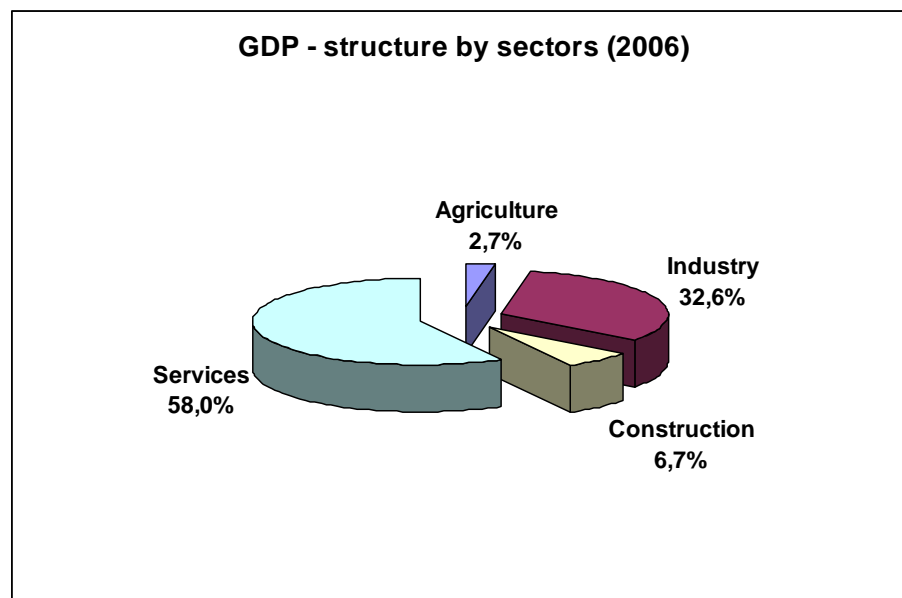
Member of the European Union: since 1st May 2004.

Macro economic indicators

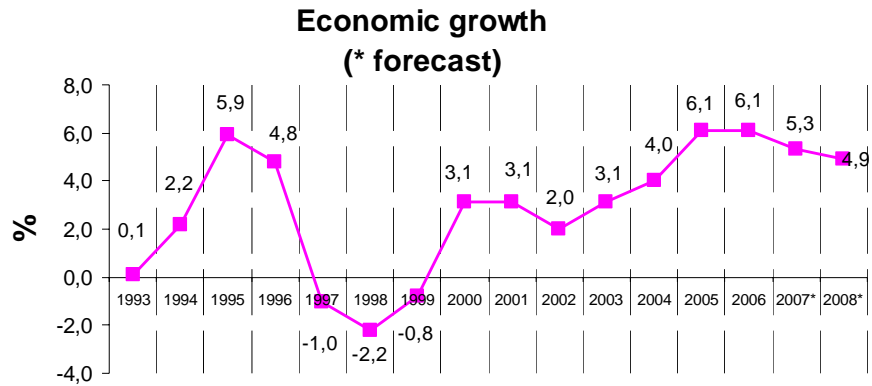
Gross domestic product and economic growth

The gross domestic product of the Czech Republic in nominal values for 2006 was USD 153.48 billion (CZK 3.204.10 billion), which represents a year-on-year growth (in crowns) of 7.87%.

In 2006 the GDP per capita was USD 14,950 (CZK 312,087).



The following graph depicts the development of real GDP during recent years and expected development in the coming period, according to the EUROSTAT the figures of the GDP result from base of the year 1995.



Unemployment

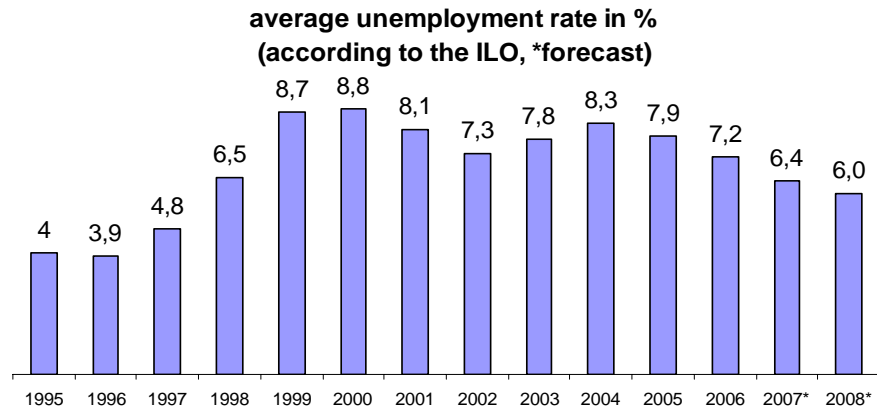
The number of unemployed at the end of 2006 was 474.8 which represented a decline of 7.7% on 2005.

According to the International Labour Organisation's methodology the average unemployment rate at the end of 2006 was 7.2 %.

There are relatively significant differences between individual regions.

The lowest rate of unemployment is consistently in the capital of the Czech Republic - Prague – at approx. 3%, whilst the highest rate of unemployment is in former centres of heavy industry – at approx. 20%.

The international comparison outputs confirm that the rate of unemployment in the Czech Republic has been below the EU average in the long term.



Average wages

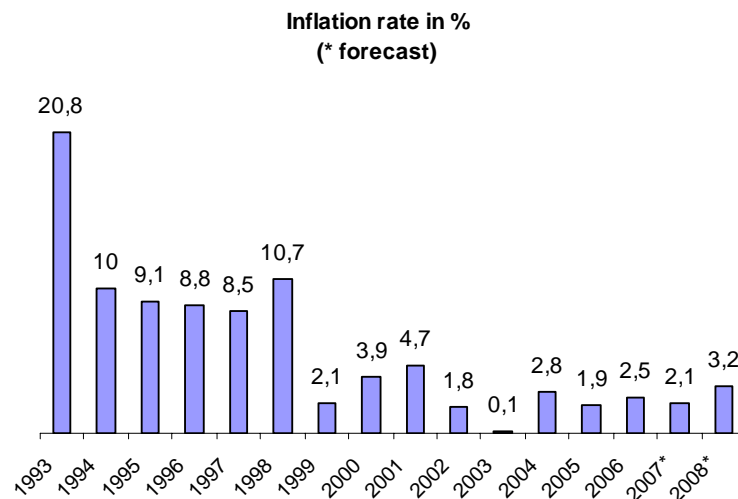
The average nominal monthly wage earned in the private sector in 2006 was USD 973.96 (CZK 20,333). This represents a wage increase of 6.8% on 2005. In real terms, wages grew by 4.2% in 2006,

The national average monthly wage for 2006 was smaller than for the private sector, coming in at USD 968.11 (CZK 20,211), which represents a year-on-year nominal growth of 6.5% and growth in real terms of 3.9%.

Inflation and interest rate

The inflation rate in 2006 was 2.5%, which represents a decrease of 0.6% on 2005.

Economic forecasters predict that the price level in the Czech Republic in coming years will grow at roughly the same rate as in 2005. They also predict that the inflation rate will reach 2.1% in 2007, and 3.2% in 2008.



The high inflation rate in 1993 was a result of the tax reforms introduced after 1st January 1993.

Interest rate

Some key rates of the CNB monetary politic have been changed this year. The last change was carried out on September 29th 2006.

Public finances

In 2005 the state budget deficit reached USD 4.7 billion (CZK 97.60 billion), i.e.: 3.0% of GDP, which represents a year-on-year decline of CZK 41.30 billion.

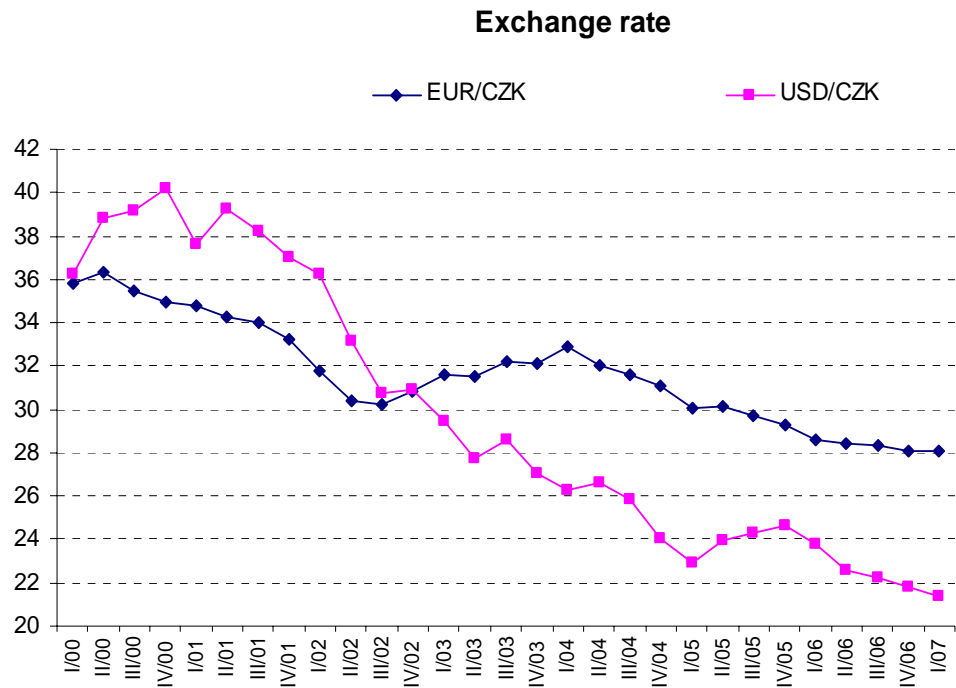
Public debt reached USD 38.44 billion (CZK 802.5 billion) at the end of 2006, which represents a 25% share of gross domestic product. In 2005 the debt rate was lower at 23.30% share.

Currency

The Czech crown has been a convertible currency since October 1995.

In May 1997 the fixed exchange rate system was dissolved. The currency's new floating exchange rate is now determined by supply and demand on the currency market. The central bank has the right to employ monetary instruments (intervention on the currency market, etc.) to influence the crown exchange rate (a so-called dirty float). The decisive factor of the central bank's exchange rate policy is the relationship of the Czech crown to the Euro.

The long-term exchange rate of the crown to the Euro and to the USD is depicted in the following graph.



The crown exchange rate (monthly average as published by the central bank, April 2007) is:

CZK/USD: 20.731, CZK/EUR: 28.010

Balance of payments and foreign debt

In the long run the Czech Republic's balance of payments is characterised by a current account deficit financed by a significant surplus on the financial account (foreign capital inflows, which in the last few years have been mainly in the form of direct foreign investments).

The central bank's foreign currency reserves grew by USD 1.89 billion during 2006, reaching USD 31.45 billion by the end of the year.

At 31st December 2005, the level of foreign currency reserves was enough to cover an average of 4.6 months' worth of goods imports, which means that foreign currency reserves are in the 'safe' band i.e. the state's official foreign reserves of at least three months' worth of imports.

The development of gross foreign debt in 2006 was confirmed by the trend of long-term growth (CZK 1,217.00 billion, i.e. USD 58.30 billion.). Foreign debt grew by CZK 74.8 billion year-on-year, i.e. at an increase of 6.6%. The level of foreign debt was 38.0% of GDP (37.8% of GDP at the end of 2005), therefore remaining below the generally accepted 'safe' limit of 40%.

Business sector debt accounts for the decisive portion of foreign debt (roughly 56% without taking the debts of commercial banks into account).

The public sector's foreign debt reached approximately 20%.

3. Foreign investment

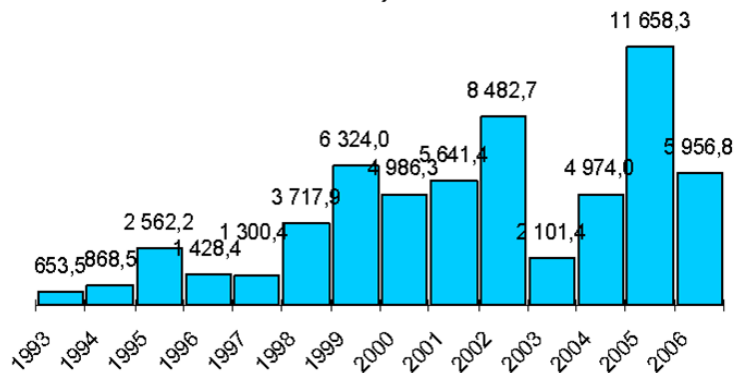
The Czech Republic is a net importer of capital - in the form of direct foreign investments.

The period since 1998 is characterised by high inflows of direct foreign investments; the highest annual value during the past 10 years was recorded in 2002. Exceptional development in 2003 - a significant decline in foreign direct investments - was due to the repurchase of shares in large Czech telecommunication companies from foreign owners.

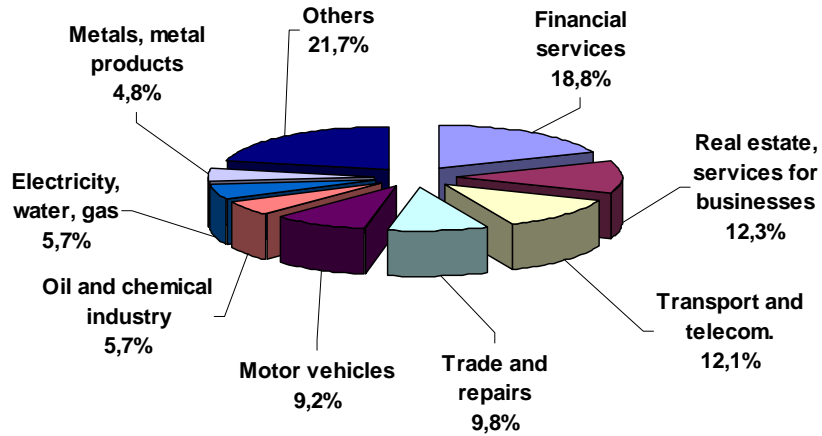
The inflow of foreign direct investments in 2006 was USD 5.96 million (CZK 134.68 million), which corresponds to 4.2% of GDP.

The total value of foreign direct investments into the Czech economy at 31st December 2006 reached USD 66.619 million (CZK 1,626.24 million) = 50.76% of GDP.

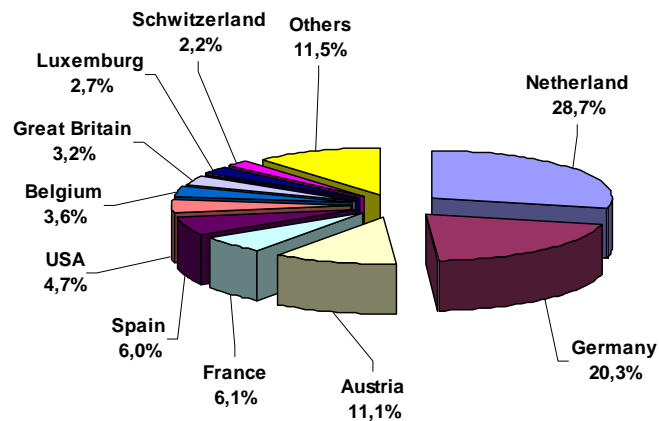
Inward Foreign Direct Investment (in millions of USD)



Structure of FDI by sectors at 31st December 2005



Structure of FDI by country at 31st December 2005



Investment incentives

Since 1998 the Government of the Czech Republic has used active instruments to support the inflow of direct foreign investments according to pre-set criteria. Since May 2000, the statute guarantees entitlements to the allocation of investment incentives for investment projects in the processing industry.

Investment incentives are designed for foreign, as well as Czech, investors and are aimed at the introduction and expansion of production capacity in the processing industry and for projects in the area of strategic services and technological centres.

Investment incentives in the processing industry stipulated in the Investment Incentives Act are designed for the following investment projects (all of the stipulated conditions must be met at the same time):

- Greenfield and Brownfield investment – launch of new production capacity or expansion of existing production capacity; modernisation of production to make significant changes to the product or the production process;
- The minimum amount invested into fixed tangible and intangible assets (not including leased assets) is CZK 200, CZK 150, CZK 100 million, depending on the unemployment rate in the given region (see table below);
- At least one-half of the stipulated minimum investment for the given region must comprise the investor's own capital;
- At least 40% of the total amount invested must be spent on highly advanced machinery;
- The above conditions must be met within three years of the granting of the incentives;
- The recipient of the investment incentives must not start work on the project before submitting the investment incentive application with CzechInvest (a state agency for the promotion of business and investments in the Czech Republic);
- The recipient of the investment incentives must maintain the investment, in respect of which the incentives were granted, for at least five years from meeting the above conditions;
- The recipient of investment incentives granted in the form of material support for work positions must retain these newly created work positions for at least five years of the first drawing on the investment incentives;
- The recipient of the investment incentives must be the first owner of the fixed tangible assets (e.g. machinery) in the Czech Republic, except in the case of real estate; and
- The production process employed must be environmentally friendly.

Current investment incentives granted pursuant to the Investment Incentives Act are shown below.

Tax holidays

- Full relief from income tax for up to 10 years is available for newly established companies; and

- Partial relief from income tax for up to 10 years is available to existing companies implementing an investment plan.

The investor is entitled to exercise the tax relief claim only upon meeting conditions for granting the investment incentives, not later however than three years from their granting. Tax holidays shall start not later than three years after the granting of the investment incentives, regardless of the company's financial results. If the investor meets conditions for the granting of the investment incentives, e.g. immediately in the first year of their granting, he/she can start exercising the tax holidays immediately, or wait until the third year of the grant.

Material support for work creation

CZK 100,000 or CZK 200,000 is available per work position created, depending on the unemployment rate in the region.

Additionally, there is a contribution of CZK 25,000, if the investor gives the newly created work position to someone with a medical disability or an applicant for work posted at the labour office.

Material support for re-training

This support equals 35% of the costs of re-training employees, depending on the unemployment rate in the region.

Subsidies

Subsidies are available to municipalities, regions and developers for the construction of technical infrastructure and the preparation of lots for the realisation of investment plans.

Accession to the European Union (EU)

The Agreement on the Accession of the Czech Republic to the EU, along with other candidate countries, was signed in Athens on 16th April 2003. On the basis of this Accession Agreement the Czech Republic became a member of the EU on 1st May 2004.

Upon acceding to the EU, the Czech Republic gained the opportunity to draw on resources made available by the EU from its structural funds, the solidarity fund (or other funds) under the same conditions as other EU member states.

With regard to the subsidies of business development funded from the EU structural funds, there plans for three operating programmes for the period 2007 – 2013:

- Business and innovation

- Business and innovation environment
- Services from the business development

The state administrative authorities responsible for the utilisation of funds from the EU are the Ministry of Local Development of the Czech Republic and other ministries, into whose competence the specific projects fall. Basic information and contacts may be obtained at:

www.strukturalni-fondy.cz, www.czechinvest.cz, www.mpo.cz

Banking system

A two-tier banking system was established in 1990 - a central bank and a network of commercial banks.

In the Czech Republic the central bank is called the Czech National Bank (Česká národní banka – ČNB). The rate of compulsory minimum reserves has been set at 2% since 1999.

Foreign banks may establish branches in the Czech Republic without limitation. Banks owned by foreign entities are subject to the same rights and obligations as domestic banks.

4. Setting up a Business

Types of business

A foreign person may opt for various types of business on the territory of the Czech Republic. Investors are obliged to follow Czech legal regulations during the execution of their business activities.

Entrepreneur – natural person

The Act to Regulate Trades allows a foreign natural person to undertake business on the territory of the Czech Republic under the same conditions as those that have to be met by a resident of the Czech Republic. Trade can be carried out by an entrepreneur – a natural person or through an authorised representative.

A foreign natural person, who is a citizen of an EU country, the European Economic Area, or Switzerland, is not required to submit a residence permit valid on the territory of the Czech Republic.

A residence permit on the territory of the Czech Republic is required with other natural persons, except for a foreign person undertaking trade on the territory of the Czech Republic through a branch.

A foreign natural person has to enter in a commercial register the day of becoming authorised to carry out business on the territory of the Czech Republic. This does not apply to foreign persons from the EU or from other countries of the European Economic area.

Foreign person's organisation section

A foreign person may establish an organisation section on the territory of the Czech Republic. A foreign legal entity is authorised to undertake the business on the territory of the Czech Republic upon the entry of its organisation section in a commercial register. An organisation section is not an independent legal entity.

A foreign legal entity must appoint an authorised representative who meets conditions for carrying on trade.

A foreign legal entity is represented by the manager of its organisation section (in matters regarding this organisation section) in contact with third parties.

Only profits achieved on the territory of the Czech Republic are subject to income tax. A different tax determination method than a standard method applied to Czech business companies can be agreed with a tax office (e.g. tax based on a cost level – 'Cost Plus').

Business companies

The Commercial Code differentiates several types of business company:

- An unlimited liability company
- A limited partnership company
- A limited liability company
- A joint-stock company

The most frequent are limited liability companies and joint-stock companies.

A foreign person may be a member in a Czech business company – a company with a registered base in the Czech Republic.

A business company is a legal entity established on the day it is entered in a commercial register. In contact with third parties, it is represented by a statutory body. The legal entity carries out trade through an authorised representative.

Unlimited Liability Company ('v.o.s'.)

An unlimited liability company is a company in which at least two people carry on the business under the same corporate name. Both a legal entity and a natural person can be its member. Members guarantee the company's obligations jointly with their assets.

The law does not prescribe an obligation to create basic capital.

Profit or loss is divided among members according to a Memorandum of Association.

The members are a statutory body.

The profit of an unlimited liability company is subject to income tax of individual members under the scope of their tax returns. An unlimited liability company itself is not subject to legal entity income tax.

Limited Partnership Company ('k.s'.)

A limited partnership company is a mixed type of Limited Liability Company and unlimited liability company, combining features of both. In a limited partnership company, a limited partner guarantees the company's obligations up to his contribution (similar to a member in a limited liability company) and at least one limited partner guarantees it with all of his assets (similar to a member in an unlimited liability company) (general partner). A legal entity can be a limited partner.

Profit is divided among limited partners according to a Memorandum of Association.

General partners are a statutory body.

The general partner's profits are subject to income tax as part of their tax returns. Limited partners' profits are taxed as the company's income in the form of legal entity income tax, and the limited partners may be subsequently paid shares in profit.

Limited Liability Company ('s.r.o.')

A limited liability company is a company whose basic capital is created by members' contributions. The members guarantee the company's obligations up to the amount of their contributions. Basic capital must be at least CZK 200,000, whereas one member's contribution must be at least CZK 20,000.

A limited liability company can also be established by a sole person. A limited liability company with a sole member can be the only founder, or the sole member, of another company. One natural person may be a member in at most three limited liability companies. The company may have a maximum of 50 members.

The company guarantees the company's obligations with all of its assets.

The members take part in profit according to the ratio of their contributions to basic capital, unless specified otherwise by a Memorandum of Association.

A corporate agent or agents are statutory body acting on behalf of the company.

The company's profit is subject to legal entity income tax.

Joint-stock company ('a.s.')

A joint-stock company can be established by one person provided that the founding person is a legal entity; in other cases, it must be established by at least two people.

The basic capital of a company established with a public offer must be at least CZK 20 million; otherwise, basic capital must be at least CZK 2 million. The company's basic capital is divided into a certain number of shares.

The company guarantees its obligations with all of its assets. A shareholder is not held liable for the company's obligations.

A shareholder is entitled to a share in the company's profit (dividend) approved by a general meeting.

Shareholders form a general meeting that is the supreme body of the company. The general meeting takes place at least once a year, no later than within six months of the last related financial period.

The company's statutory body is a Board of Directors that manages the company's activities and acts on its behalf. The Board of Directors is controlled by a Supervisory Board. The Board of Directors and the Supervisory Board must have at least three members.

The company's profit is subject to legal entity income tax.

Co-operative association

A co-operative association is an association of an open number of people established for the purpose of common business, or of securing its members' needs.

A co-operative association must have at least five members, or only two members who are legal entities.

Members are not held liable for the co-operative association's obligations while the co-operative association guarantees its obligations with all of its assets.

The co-operative association's basic capital is from member deposits and must be at least CZK 50,000.

The supreme body of the co-operative association is its members' meeting that meets at least once a year.

Activities of the co-operative association are managed by a Board of Directors, a statutory body. Activities of the co-operative association are controlled by an inspection committee.

The co-operative association's profit is subject to legal entity income tax.

Capital interest – dormant partnership

Based on a dormant partnership agreement, a dormant partner participates in business activities by means of a pecuniary or non-pecuniary contribution. The dormant partner has his share in economic results (profit and loss) agreed upon in the agreement. The dormant partner participates in loss up to the amount of his contribution.

The dormant partner's incomes are subject to deduction tax in the Czech Republic.

5. Labour

Effective as from 1 January 2007, a new Labour Code was approved, Act N 262/2006 Coll. The new Labour Code is based on principle “what is not banned is permitted” and follows the valid Civil Code according to the fact that in employment relations also appropriate paragraphs may be applied.

Employment contract

Every employer is obliged to sign a written employment contract with its employees.

The employment contract must contain:

- The type of work to be performed
- The place or places of work
- The starting date

Probation period

The probation period must not exceed three months. The probation period must be arranged in writing; it cannot be arranged subsequently and its duration cannot be altered later. The new Labour Code (from Jan 1, 2007) has changed the way of counting the probation period. The probation period starts one day after the beginning of employment relation. The last day of probation period is the day which is numerically equal to the day of event since the period has started. If the last day of probation period is Saturday, Sunday or state holiday, then it is the nearest following working day. Time of impediment to the performance of occupation, during which the employee cannot do his/her work within the probation period, is not added. So the time of impediment to the performance is not the time of probation and therefore the probation time is extended in due course. These shifts will the employee have to do after the originally stated time of probation.

Termination

The employment may be terminated:

- By agreement
- By notice
- By immediate termination of employment
- By termination within the probation period
- By expiry of the employment relation
- If a foreign employee is deprived of his/her residence permit or deported and newly the end of working permission validity
- By death of an employee

Both the employer and employee may terminate the employment unilaterally.

The term of notice starts on the first day of the calendar month following the month when the term of notice was delivered to the other side, and expires with the last day of the relevant calendar month.

Since the amendment of the Labour Code the term of notice is stated to be two-months, with the possibility to discuss a longer term (the same for both counterparts).

Notice of dismissal served by an employee:

- May be served without stating any reason
- Two months' period of notice must be given

Notice of dismissal served by an employer:

- The reasons for notice must be stated at all times and there is full list and it cannot be extended.

The notice may only be served to the employee for the following reasons:

- The company (or large part thereof) ceases to exist or is transferred elsewhere (term of notice: two months, severance pay equals average salary for three months);
- Redundancy of the employee due to company decision to change its activities or technical resources, reduce human resources or achieve higher work productivity (term of notice: two months, severance pay equals average salary for three months);
- Organisational changes (term of notice: two months, severance pay equals average salary for three months);
- Due to the health state (certified by a medical opinion or a state administration body) the employee is no longer able to perform his/her current work (term of notice: two months). If working is unable due to working injury, disease, occupational disease threat or the highest possible exposure, severance pay equals twelve times the average monthly salary;
- The employee does not fulfil work performance prerequisites (term of notice: two months); or
- Gross breach of the work discipline. The employee must have received reprehension regarding possible notice within the past six months. In the case of continuous minor breaching of the work discipline (term of notice: two months).

Prohibition against serving of a notice applies:

- During a period in which the employee is approved temporarily incapable of work due to sickness or an injury;
- If the employee performs a public function; or
- If the female employee is pregnant or on maternity leave.

Immediate termination of the employment relationship:

- The employee may terminate the employment immediately when he/she is no longer able to perform work without a serious threat to his/her health according to a medical opinion, and the employer has not transferred him/her to another suitable work position within 15 days of the submission of the medical opinion;
- The employer has failed to pay the employee wages within 15 days of the due date. The employee is entitled to get severance pay; or
- The employee who immediately cancelled his/her employment contract has the right to claim wage compensation in the amount of his/her average salary for the duration of the term of notice.

The employer may immediately terminate the employment relationship only in exceptional cases, if:

- The employee is validly convicted by a court of law for an intentional criminal act and subject to an unconditional prison term of one year or more; or, in the case of an intentional criminal act committed during work performance, was placed to unconditional prison for a minimum of six months; or
- The employee breached work discipline in an exceptionally gross manner.

The employer may immediately terminate the employment relationship only within one month from the day when he/she learned about the grounds for immediate termination, however at the latest within one year of the day when these grounds arose.

Within the probation period both the employee and employer may terminate the employment relationship for any reason, or without stating any reason whatsoever.

Work performance

Exceptionally, apart from employment contracts, citizens may also conclude agreements on work performance outside the employment. Newly these agreements have to follow the statement of the minimum wage.

- The 'agreement to complete a job' may be signed if the expected scope of work does not exceed 150 working hours for the calendar year. This

agreement is not subject to social security and health insurance payments.

- “The work performance agreement” The average working hours must not exceed on average half of the weekly working hours.

Annual leave

The statutory period of annual leave is four weeks. This period may be extended by further days and weeks according to internal regulations.

Employees are entitled to wage compensation equal to the average salary during annual leave.

By the Labour Code amendment some new changes have been implemented:

Application of working time account – indicating a different way of layout of the working time. It is compulsory to keep the account of working time and wage account of the worker by the employer. By this means stated working time of the worker to the working time already realised is compared. The wage account shows regular wages already paid and also entitlement to wages to be paid. The compensatory period must not exceed 26 weeks following each other.

Work readiness can be realised only out of the working place The readiness kept on the working place, when the employee is ready to work for the employer, is included in the working time.

Extra pay for working on Saturday and Sunday is also claimed in business environment – 10 % of the average salary, extra pay for night work has changed from 6,- CZK per hour to 10 % of the average salary, extra pay for work in difficult working environment – 10 % of the average salary. Extra pay for working overtime remains unchanged – 25 % of the average salary and extra pay for working during state holiday 100 % of the average salary.

The new Labour Code does not make it possible to include overtime to salary. For working overtime the employee gets salary he/she is entitled to for the time worked off and extra pay minimum 25 % of the average salary, if the employer has not made an agreement with the employee on providing time off as compensation in the extent of working overtime instead of the extra pay.

Remuneration

The minimum wage, valid from 1 January 2007, is stated to be 8000.00 CZK per month for 40 working hours per week (i.e. 48.10 CZK per hour).

The employer may establish any remuneration system with or without wage tariffs, different forms of wages (hourly, task, proportionate, combined etc.) and may introduce various wage components or parts (bonuses, awards, extras, the so-called 13th and 14th salary). The Labour Code introduces a term of guaranteed wage, which is the employee entitled to according the Labour Code, contract, internal instruction, state of remuneration.

Average salary

Average salary is calculated from the gross wages remunerated to the employee during a decisive period (principally the previous calendar quarter) and from the time the employee worked during this period. The average salary is calculated on the first day of the calendar month after the decisive period i.e. on 1 January, 1 April, 1 July, 1 October.

Natural person income tax (generated from employment and functional benefits)

Income from employment includes all income received by the employee from the employer within a calendar month based on:

- The employment relationship;
- Income received by partners or executives of limited liability companies and income received by members of co-operatives; and
- Benefits to members of statutory bodies and other bodies of legal entities paid from the profit earnings for work on boards (board of directors) or supervisory boards, the so-called royalties.

Tax contributions or advance payments on tax from the above incomes are paid by the person who pays the income. In a case where the payer has not submitted the signed 'Declaration of the taxpayer of natural person income tax from the employment and functional benefits' to the payer/employer of the tax contribution, the rate, set for income not exceeding 5,000 CZK per month, is 15%.

In the case of a tax non-resident hiring employees to work in the Czech Republic, the so-called international workforce hire, for the purposes of income tax determination, the income paid is considered as income paid by the payer. In the case of the payment to a person domiciled abroad, it also includes the fee for hiring. Such an employee is considered to receive income in the amount of at least 60% of the entire payment he/she received.

Non-monetary benefits are also taxed. For example, in the case of a car provision, free of charge and also for private purposes, the employee's income is 1% of the market entry price of the car per calendar month.

Tax base is income from dependent activity reduced by social security and health insurance which an employee is obligated to pay. For employees that are obligated to pay foreign insurance, the income is reduced by this foreign insurance. The monthly wage tax advance is calculated from this tax base. This monthly wage tax deduction is reduced by individual tax allowances.

Tax allowances

Tax allowances are:

- 600- CZK monthly allowance for taxpayer
- 4,200- CZK per year for wife/husband, whose yearly income is not higher than 38.040.- CZK
- 125- CZK monthly allowance if the taxpayer is partly-invalid
- 250- CZK monthly allowance if the taxpayer is fully-invalid
- 800- CZK monthly allowance if the taxpayer has the ZTP/P card
- 200- CZK monthly allowance if the taxpayer is student not older than 26 years, for Phd. programmes not older than 28 years

The below stated items are taken in consideration at the end of year with in the yearly settlement:

- Gifts
- Interest on loans paid within the taxable period
- Pension insurance contribution
- Private life insurance contribution paid within the taxable period
- Deduction of trade union membership contributions
- Deduction of payment for exam – new from Jan 1st 2007, it is possible to deduct payments for exams checking the results of further studies from the tax base in the taxation period according to the Law on Checking and Accepting Results of Further Studies if they were not paid by the employer or were not claimed as outcome. Yearly the amount of maximum 10,000- CZK can be deducted, with handicapped taxpayer it is maximum 13,000- CZK and with more serious handicapped taxpayer maximum 15,000- CZK.

Tax Allowance

Starting in 2005, the taxpayer is entitled to a tax allowance for a dependant child living in the household (previously a tax deduction).

Tax allowances may be used in the form of tax reduction, tax bonus or a combination of both.

The amount of tax allowance is 500 CZK per month per child.

Employment of disabled persons

Every employer with more than 25 employees must employ people with a health impairment. The compulsory proportion is 4%. The employer may fulfil this obligation by:

- The employment relationship
- Using products or services of employees who employ more than 50% of employees with health impairments
- Contribution to the state budget

Employment of foreigner employees (foreign nationals) and employment of EU citizens

The Employment Act defines citizens of other than UK countries as foreign employees.

Employers may only employ foreign employees with a work permit from a relevant labour office. Applications are submitted to the labour office according to the place of work performance. A foreigner may obtain the work permit only if the job vacancy cannot be filled by a job seeker. As a priority, referred job vacancies are first offered to Czech citizens, then to EU citizens, while the foreigner may only receive the work permit if the vacancy remains unfilled after this procedure.

The work permit is issued for a fixed maximum period of one year and may be extended.

A foreigner working for a business company as a partner, or as a member of a statutory body of a business company, and when the work he/she performs is the subject of business activity of the company, he/she does not require the work permit.

All foreigners who are required to obtain the work permit, as well as EU citizens who are not required to obtain the work permit, must be registered at the labour office.

The employer of EU citizens has a duty only to inform the labour office of employing EU citizens, within 10 days of the day the work starts.

A foreigner, who is transferred to work in the Czech Republic, in accordance with a contract with a Czech legal entity, requires the work permit.

Health insurance

Public Health Insurance is compulsory for people who:

- Are permanently resident in the Czech Republic; or
- Are not permanently resident in the Czech Republic, but are employed by an employer with a business registered in the Czech

Republic (while taking into account new circumstances related to the accession of the Czech Republic to the EU, e.g. determination of the legal allegiance in the case of collateral performance of profit-making activity in two or more EU member states).

Among the key EU principles is the 'one insurance principle', e.g. at any time an insured EU citizen is subject to legal regulations of one member state and therefore is insured in the state in which he/she performs the profit-making activity.

The 'one insurance principle' does not apply in certain cases if the profit-making activity is performed in more than one state. Therefore, an employee resident in another EU state, who works for an employer in the Czech Republic and also performs another profit-making activity in its domicile state, is insured in the country of residence, and the Czech employer pays his/her insurance to the competent insurance company in his/her state of residence. The insured must submit form E101, which documents his/her allegiance to legal regulations of another state.

The health insurance does not apply to people who:

- Are non-resident in the Czech Republic and work in the Czech Republic for employers not registered in the Czech Republic;
- Live abroad long-term and do not pay the insurance; or
- Are non-resident in the Czech Republic and work in the Czech Republic for employers with diplomatic immunity and benefits.

Compared to the previously valid legal regulation, people without permanent residency in the Czech Republic who work for an employer according to foreign legal regulations must participate in the public health insurance and are therefore obliged to pay its premiums as employees.

Citizens insured by public health insurance enjoy basic rights, mainly:

- The right to complex healthcare in the Czech Republic;
- The right to necessary healthcare in EU member states;
- The right to healthcare without direct payment, if provided to the extent and according to conditions set out by law; and
- The right to medical products without direct payment, if such products are covered by the health insurance.

Social security, sickness benefits and pension insurance

Payers of social security premiums are employers, e.g. the organisations/ legal entities or natural persons that employ at least one employee, and employees participating in the health insurance (i.e. working in the Czech Republic).

The provision of 'one insurance' also applies to this type of insurance – an employee working in two or more states may be insured only in one state.

In such cases priority lays with the insurance of the state of his/her residence. The employer pays social security premium to the state where his/her employee is domiciled. Such insurance is paid according to regulations of the state where the employee is insured (see compulsory E101 form referred to above.)

Health insurance benefits

Sick-pay

Provided for calendar days, at no more than:

- 160- CZK - for the first three days of sick leave.
- 441- CZK - from the 4th to the 14th day of sick leave.
- 479- CZK - after the 15th day of sick leave.

Support to care for a sick family member

This support is paid to an employee who cares for a child, or other sick family member, whose state of health requires the necessary attendance of another person. It is provided for nine calendar days (or, for 16 calendar days to a single person).

Maternity pay

The basic period of maternity pay is 28 weeks (to a married woman) provided required conditions are fulfilled.

Compensatory pregnancy and maternity bonus

The purpose is to balance the difference between wages of a pregnant employee before she was transferred to another work due to her pregnancy.

Pension scheme

Providing the statutory requirements are fulfilled, this insurance scheme guarantees pension insurance benefits to the employee.

This includes:

- The retirement pension. Determining factors for the retirement pension benefit include the length of the pension insurance, the age required for the entitlement to the pension, and the income earned during the period under review;
- The full and partial disability pension;
- Orphan's pension; and
- Widow's and widower's pension.

The pension insurance scheme is to undergo a complete reform soon.

The base for the pension insurance contribution calculation is the gross income of the employee. There is no maximum assessment base. The rate is proportionate.

	Contribution	
	Employer	Employee
Health Insurance	9.0%	4.5%
Social Security	26.0%	8.0%
Total	35.0%	12.5%

Becoming effective on January 1st 2007, there are some other single changes:

- Application forms for getting pension will be always filled in by the Institute of Social Security; and
- The rate of penalty on insurance owed has been changed from 0.1% for each day of delay to 0.05% for each day. In part- payments from 0.05 % to 0.025 %.

The change is according to the Act N 264/2006 Coll., so called accompanying law to the Labour Code, by which the clause on calculation base for paying social security and health insurance has changed.

The calculation of the employees' insurance contribution is the total of income which is the concern of Natural Persons Income Tax according to Income Taxation Act and which is not given freedom of this tax and is provided by the employer according to the job which entitles to participation in health insurance and pension scheme.

Exceptions are these kinds of income:

- damages compensation according to the Labour Code
- severance payment and other severance payments provided on the base of special legal regulations (the Labour Code)
- single social help provided to employee for overcoming his/her extraordinary difficult situation created as natural disaster consequence, ecological or industrial accident or other extraordinary weighty events

- fulfilments provided after the end of the job if fulfilment is provided to life anniversary or other anniversary or deserves award and the reason for providing of this fulfilment arose after the end of job
Statutory insurance of the employer for liability for damage (in the case of a work injury or occupational disease)

The liability insurance of employers is statutory, i.e. it is established according to the establishment of the first employment relationship, without any insurance contract. No insurance contract is signed and possible failure to pay premiums does not affect the validity of the insurance, or claims of employees for indemnification for a work injury or occupational disease.

The base of the statutory insurance is the legal right of the insured employer that the relevant insurance company compensates for damage suffered by its employee, a work injury or an occupational disease, within the extent of the employer's responsibility according to the Labour Code.

The premium rate is set according to the predominant subject of the employer's work as registered in the Commercial Register and is in amount of 2.8 – 54.4 per mille of the base for calculation of social security premiums. The minimum premium is 100 CZK per calendar quarter.

Penalties for failure to pay the compensation insurance are severe. If the premium is not paid duly and on time, it is increased by 10% of the owed amount for each new month started thereafter.

6. Taxation

The Czech tax system, newly created in 1993 and valid since then, includes direct tax (income, property), indirect tax (consumption) and other taxes (insurance and social security). Since their creations, tax regulations have been, and still are being, much modified; the latest significant changes are related to the accession of the country to the EU and harmonisation of the national legislation with EU directives.

Tax administration

Tax contributions are collected and controlled by tax offices, according to the residency of people subject to the tax. A total of 222 tax offices are supervised by financial directorates that manage activities of tax offices and decide on appeals filed by taxpayers against tax offices. The eight financial directorates are based in former regional cities.

The highest tax administration authority is the Ministry of Finance, which decides corrective measures against financial directorates, methodically manages each directorate and integrates tax administration procedures.

A decision of the appellate body (a financial directorate or the Ministry of Finance), which is at variance with the law, may be taken to court. However, the court decision is binding only with regards to each particular case and does not create a precedent. The appeal or suit has no dilatory effect, which can cause problems as the court procedure may take several years.

In the case of fiscal evasion, tax is corrected including a penalty of 0.2% for each day of delay from the arrears of tax. Rules that apply in the case of tax proceedings bind the taxpayer, and not the tax office, to prove the correctness of the tax duty calculation, and the burden of proofs lies with the taxpayer. Unless the taxpayer can prove his/her expenses, the tax office increases the tax base and sets out the arrears of tax and penalty.

If the tax office decides it was a case of intentional tax evasion, it may take legal action. If the court proves intentional fiscal evasion it imposes charges according to accrued damages.

Avoidance of double taxation

One of the tax system principles is the superiority of international treaties over national regulation.

The Czech Republic has ratified the treaty on avoidance of double taxation with the following states:

Albania, Australia, Azerbaijan, Belgium, Byelorussia, Brazil, Bulgaria, China, Denmark, Egypt, Estonia, Philippine, Finland, France, Croatia, India, Indonesia, Ireland, Island, Italy, Israel, Japan, JAR, former Yugoslavia, Canada, Kazakhstan, South Korea, North Korea, Kuwait, Cyprus, Lebanon, Lithuania, Latvia, Luxemburg, Hungary, Macedonia, Malaysia, Malta, Morocco, Mexico, Moldavia, Mongolia, Germany, Nigeria, the Netherlands, Norway, Poland, Portugal, Austria, Romania, Russia, Greece, the United Arab Emirates, Singapore, Slovak Republic, Slovenia, Serbia and Montenegro, Sri Lanka, Spain, Sweden, Switzerland, Thailand, Turkey, Tunisia, Ukraine, the United States, Uzbekistan, the UK, Venezuela, Vietnam.

A summary of selected treaties and taxation of dividends, interests and licences duty, generated from sources in the Czech Republic, is as follows:

State	Valid from	Maximum tax rate in the source country		
		Dividends	Interests	Licence fee
Australia	27.11.95	5% for share of min. 20%, otherwise 15%	10%	10%
France	1.7.2005	0% for share of min. 25%, otherwise 0%	0	10%/ 5%/ 0%
Ireland	21.4.96	5% for share of min. 25%, otherwise 15%	0	10%
Italy	26.6.84	15%	0	5%/0%
Japan	25.11.78	10% for share of min. 25%, otherwise 15%	10%	10%/0%
Canada	28.5.02	5% for share of min. 10%, otherwise 15%	10%	10%
Cyprus	30.12.80	10%	10%	5%/0%
Luxembourg	30.12.92	5% for share of min. 25%, otherwise 15%	0	10%/0%
Hungary	27.12.94	5% for share of min. 25%, otherwise 15 %	0	10%
Germany	17.11.83	5% for share of min. 25%, otherwise 15%	0	5%
The Netherlands	5.11.74	5% for share of min. 25%, otherwise 10%	0	5%

Poland	20.12.93	5% for share of min. 20%, otherwise 10%	10%	5%
Austria		10%	0	5%/0%
Russia	18.7.97	10%	0	10%
Slovak Republic	14.7.03	5% for share of min. 10%, otherwise 15%	0	10% /0%
Switzerland	23.10.96	5% for share of min. 25%, otherwise 15%	0	5%
United States	23.12.93	5% for share of min. 10%, otherwise 15%	0%	10%/0%
UK	20.12.91	5% for share of min. 25%, otherwise 15%	0	10%/0%

Ratified treaties employ two methods of double tax avoidance – exemption of foreign incomes from the taxation or credit of the tax paid abroad.

Direct taxes

Legal entity and natural persons' income tax

Natural persons' residence in the Czech Republic, or people who are living in the country for more than 183 days in the calendar year, are tax residents of the Czech Republic. Worldwide incomes of such people are subject to taxation of natural persons' income in the Czech Republic.

Natural persons that do not fulfil the above mentioned conditions, or in cases where international treaties apply, are only taxed on the income generated from sources in the Czech Republic (restricted tax duty).

Types of incomes are:

- Income from the employment and functional benefits
- Income from business and other self-employment activities
- Income from capital assets
- Income from rentals and leases
- Other income

The following incomes from the sale of items that are not part of business assets are exempt from tax:

- Income from sale of cars, airplanes and boats, if possessed longer than one year; income from the sale of other personal assets is unrestricted;

- Income from the sale of shares in business companies, membership rights to co-operatives, if owned longer than five years;
- Income from the sale of securities within six months of receiving them; under certain circumstance income from the sale of a family house or flat, if the taxpayer has been permanently registered at the relevant address for two years before the sale; and
- Other real estate, if possessed by the taxpayer for longer than five years.

The tax base is decreased by deduction:

Title of the non-taxable amount applied	Annual deduction from the tax basis, in CZK
Gift aid	min 2% and max 10% of tax base
Interest on loans from building societies, mortgage	max. 300,000
Private pension insurance	max. 12,000
Private life insurance	max. 12,000

It is possible to reduce the final tax liability by following tax allowances:

Reason for deduction	Deduction in CZK per year
basic tax allowance	7 200
child	6 000
wife without income	4 200
partly-invalid pension	1 500
full-invalid pension	3 000
serious physical handicap	9 600
student not older than 26 years	2 400

Progressive rates for different levels of income in CZK are:

Income from	to	Tax rate
0	121200	12%
121200	218400	19%

218400	331200	25%
331200		32%

The annual tax base minus the non-taxable amounts is taxed by a progressive tax rate of between 15% and 32%:

The natural persons' tax return must be submitted within three months (or six months when represented by a tax advisor) following the end of the tax year.

Natural persons with an annual income of over 150,000 must pay advance payments on tax quarterly (by 15th March, 15th June, 15th September and 15th December) in the amount of one-quarter of the tax paid for the previous year. Natural persons with annual income between 30,000 and 150,000 must pay only one advance payment on tax (by 15th June) in the sum of 40%. Natural persons with annual income below 30,000 are exempt from advance payments on tax.

Apart from income tax, natural persons must also pay social security and health insurance premiums. (See above.)

Legal entity income tax

This tax applies to all income generated by legal entities and income from all their assets.

Tax rate

Tax rate for the 2006 tax year and following years is 24%; the tax rate for investment and share funds and pension funds is 5%.

Subject to tax

All worldwide income generated from activities of a legal entity registered in the Czech Republic is subject to legal entity income tax in the Czech Republic.

A restricted tax duty applies to legal entities registered abroad – only income generated from sources in the Czech Republic is subject to the legal entities income tax. This also applies mainly to permanent business establishments of foreign nationals in the Czech Republic.

Tax year

The taxable period is the calendar or economic year, and also the accounting period, if longer than 12 subsequent months.

Leasing

The act on Income Tax recognises two types of leasing – financial and operational leasing. In the case of financial leasing, ownership of a leased item is expected to transfer to the leaseholder after termination of the lease contract.

The lease for financial leasing qualifies as expense for tax purposes on condition that:

- The lease period is longer than 20% of the depreciation period set out by the Act on tax, however at least three years, eventually eight years in the case of a real estate lease;
- The leased item transfers to the leaseholder directly after termination of leasing;
- The purchase price of the item at the time of the lease termination does not exceed the potential tax residual price in the case of even depreciation at the lease; and
- A natural person entrepreneur includes the item into his/her business assets after termination of the lease.

Unless the lease relationship fulfils the above conditions it is considered as operational leasing for tax purposes.

Prices between allied subjects

Allied persons mean people connected by capital (direct or indirect share on the capital, or voting rights of at least 25%), or in another way (share in management, control, managed or managing persons). The created legal relationship is primarily for the purpose of tax base reduction or tax loss increase.

If prices between allied persons differ from the common market price, the tax office may adjust the tax base by such difference.

The common price for interests from loans between allied persons is considered to be 140% of the discount rate (the up-to-date discount rate is 0.5% p.a.). This does not apply if agreed interest is lower and the creditor is registered abroad or is a partner.

It is possible to ask the responsible Tax authority for Binding Opinion on price arranged between related parties. This Binding Opinion is issued as a Decision, which can only be changed by another Decision. The tax authority who issued it is bound by this decision. Request for Binding Opinion is charged for 50,000 CZK.

Under-capitalisation

If insolvency of a company, where the creditor is a person allied in relationship to the debtor and is not a bank or insurance company, exceeds the set limit 4:1 (loans with interests and loans from allied persons : equity capital) the paid interest is re-classified as dividends. Thus non-taxable expense for the income tax base calculation is established.

Depreciation according to tax law

Depreciation periods for fixed tangible assets are set out by the Act on Income Tax as follows:

Depreciated group	Depreciation period (in years)	Type of fixed tangible assets
1	3	PC and other office technology, some machinery
1a	4	Motor vehicles
2	5	Furniture, motor vehicles over 1.5t, construction machinery and equipment, agriculture machinery
3	10	Special technical equipment
4	20	Utilities equipment (water and gas pipes etc.)
5	30	Buildings, constructions, flats, water works
6	50	Hotels, administrative buildings, supermarkets, historical or cultural heritage

An entrepreneur may choose one of the following depreciation methods – either the straight-line depreciation or accelerated depreciation. The law sets time-scheduled depreciation for some items.

Fixed intangible assets with the right for use for a fixed period are depreciated during that period. Software is depreciated for 36 months, establishment expenses for 60 months, and other intangible assets for 72 months, unless the usable time is contractually restricted.

Goodwill acquired by purchase of a company – the so-called proved difference between the purchase price and the amount of value of status of

assets after deduction of accepted liabilities - is depreciated for 180 months (eventually dissolved).

Land and works of art are not depreciated.

Low-value tangible fixed assets with acquisition value below 40,000 CZK, and low-value intangible assets with acquisition value below 60,000 CZK, are depreciated in accordance with the trade legal regulations, i.e. a company determines its own depreciation plan – the depreciation period - in internal regulations on low-value tangible and intangible assets (taking into consideration the usable time of low-value tangible and intangible assets), and the appreciation value, which is the limit for accounting of low-value tangible and intangible assets in expenses. Determined accounting depreciations, eventually expenses, thus also represent a company's tax-deductible expenses.

Tax-preferred treatment of investments

When first acquiring new items of tangible investment assets, and they were acquired no later than for the tax period starting in the calendar year 2004, the tax base can be decreased by 10% (or 15%/ 20%) of the acquisition price for this asset item. If the tax-preferred treatment of investments cannot be applied as a result of tax losses (or if the tax base is zero), this must be applied during the next possible term.

This deduction does not lower the basis for the calculation of amortisation.

If the item for which the owner applied tax-preferred treatment of investments is to be leased within three years, the amount of the non-taxable investment must be taxed subsequently.

Tax-preferred treatment of investments cannot generally be applied to furniture, aircraft, and personal automobiles.

Tax-preferred treatment can no longer be applied to assets acquired during the tax period that started in 2005 and future years. However, provided that other conditions are fulfilled, increased amortisation can be applied in the first year, according to the type of business by up to 20% (agriculture) for these assets.

Tax losses

Tax losses can be claimed within the subsequent five years. A tax loss cannot be claimed if there has been a significant change in the structure of the persons or entities with direct participation in the capital or control (a change of more than 25% of the basic capital). Therefore, tax losses cannot

be transferred from one person (entity) to another; these losses cannot be compensated for even if the relevant companies are within the same group.

Legal entity income tax return

This tax return must be filed within three or six months (if the taxpayer is represented by a tax advisor or if an audit is mandatory) after the balance date.

Tax payment and advance payments on tax

The tax is due on the last day of the deadline for filing the tax return. If there is an overpayment, a separate request for a refund of the overpayment must be filed.

Advance payments for income tax must be paid by those persons or entities whose tax liability for the previous tax period exceeded CZK 30,000; payments are made half-yearly. If the tax liability exceeded CZK 150,000, advance payments are made quarterly.

Withholding tax

Certain types of income are taxed through the deduction of a withholding tax.

Regardless of whether the income is paid to a limited or unlimited taxpayer, the withholding tax must be paid at the time when the payment is made.

	Withholding tax
Dividends, partners' settlement shares, liquidation balance shares	15%
Interest on term deposits of natural persons	15%
Profits from sporting competitions not exceeding CZK 10,000, persons who carry out sport activity as their business	20%

*The rate is modified in accordance with any double taxation treaties that may exist for tax residents.

Income of limited taxpayers from sources within the Czech Republic

Only the income of limited taxpayers from sources within the Czech Republic is subject to taxation in the Republic; a list of these cases can be found in the Czech Income Tax Act.

This income includes:

- Income from activities of a permanent branch office;
- Income from employment;
- Income from technical, business, or other consulting, managerial or agency activities in the Czech Republic;
- Income from the use of real estate in the Czech Republic;
- Income from liberal professions; and
- Income of artists and athletes.

For the following payments to persons whose registered office is not in the Czech Republic, the Republic has the right of taxation in the following cases:

- Fees for the use of industrial property rights, software, know-how;
- Fees for the use of copyright;
- Profit shares, settlement shares, liquidation balance shares;
- Interest on credit, interest on loans;
- Income for the use of tangible assets in the Czech Republic;
- Compensation of members of statutory bodies and other bodies of legal entities; and
- Income from lotteries, competitions, and sporting competitions.

The tax on this income is collected through a withholding tax (final taxation) or through an assessment of tax.

Payment of capital contribution and profit to abroad

Czech entities (operations) can pay out capital contributions and profits to abroad with no restrictions. In the case of the payment of dividends, interest and liquidation shares to a parent company, a Czech company must pay withholding tax of 15%. The rate may be modified by a relevant double taxation treaty.

The transfer of a share held by an organisational unit to its foreign parent company is not subject to any withholding tax, or to any other restrictions.

Dividend payouts between parent company and subsidiary with the company seat in the Czech Republic or other EU country is exempt from taxation. Conditions for the tax exemption is prescribed legal form and

prescribed share on the original capital, and this share has to be fulfilled consistently for fixed period.

If a general meeting of shareholders decides to payout dividends after 01.01.2006, the share necessary for tax exemption is 10% and the fixed period is 12 months.

The same dividend tax exemption will be possible to use by a company that is resident in Switzerland.

Other direct taxes

Road tax

This tax applies to motor vehicles registered and used in the Czech Republic for profit-making activities. The rate is stable; for personal automobiles, it varies according to the capacity of the engine, and according to the total weight and number of axles in the case of utility vehicles.

Real estate tax

Real estate (i.e. land and buildings) is subject to real estate tax. The basis for taxation for land is the surface area of the land in square metres. In the case of the tax on buildings, the basis for taxation is the actual built-up construction area in square metres. There are various tax rates for open areas, agricultural land, and buildings.

The tax is generally due quarterly.

Paid real estate tax is considered a tax expense for the calculation of income tax.

Inheritance tax, gift tax, and real estate transfer tax

Inheritance tax and gift tax apply to transfers of property made free of charge. The tax base is the value of the transferred property. The rate is progressive according to the family relationship of the parties; the inheritance tax rate is half of the gift tax rate.

Neither inheritance tax nor gift tax is considered a tax expense for the calculation of income tax.

A valid transfer of real estate is subject to real estate transfer tax. The basis for the calculation of the tax is the purchase price, or the value of the real estate determined in an expert opinion, whichever is higher. The rate is flat and proportional; for the 2006 tax period the rate was 3%.

When paid, real estate transfer tax is considered a tax expense for the calculation of income tax.

Value Added Tax (VAT)

On 1 May 2004, when the Czech Republic became a member of the EU, Act No. 235/2004 Coll., the Act on Value Added Tax, came into effect. The Act imposed significant changes on the method of applying VAT in the Czech Republic. The Act was amended to include rules on applying VAT under the 6th Directive of the Council of the EU. The changes concerned mainly taxing of deliveries of goods and the provision of services between EU member states. (The term 'import' is used to mean transactions with third-party countries outside the EU.)

Tax rate

There are two tax rates by law in the Czech Republic– a basic rate of 19%, for most goods and services, and a reduced rate of 5%, mainly for food products, pharmaceuticals and medical materials, books and magazines.

Voluntary registration

Domestic entities and business establishments of foreign entities placed in the Czech Republic have the option of voluntarily choosing to register as a VAT-taxable person. To do this, it is necessary only to file an application with the tax office of the competent jurisdiction. Other foreign subjects can become VAT payers only when obliged to do so by law.

Mandatory registration

Registration of domestic entities

An entrepreneurial entity or entrepreneur with their registered office or place of business in the Czech Republic, or with permanent residency or the place in which they reside most often in the Czech Republic, that achieved a turnover of CZK 1,000,000 during a period of no more than the 12 previous consecutive months, must register as a VAT-taxable person with the relevant tax office within 15 days after the last day of the month in which this turnover was exceeded.

Example: For registration under the new Act on VAT, a turnover of CZK 1,000,000 or more should be monitored from May 1st, 2004. Therefore, if a company achieves this limit during May to August 2004, it must register as a VAT-taxable person with the tax office of the competent jurisdiction by September 15th 2004.

Registration of foreign entities (countries within EU and out of EU)

Foreign entities without their registered office or place of business or other branch office in the Czech Republic, i.e. entities that are not authorised to carry out business activities in the Czech Republic and that do carry out business activities in another member state or in a third country, are obliged to register as a VAT- taxable person. In these cases, the turnover is not the decisive factor – the foreign person must register as a VAT-taxable person when starting business activities in the Czech Republic.

Exemptions:

- Delivery of services and goods including installation and assembly; if a foreign entity delivers services or goods including installation and assembly to an entity that is subject to the tax, the foreign entity is exempt from the obligation to apply the tax; or
- Mail order sales of goods; foreign persons that deliver goods in the Czech Republic by mail order, i.e. by sending or transporting themselves, or at their own cost, goods from a member state other than the state that is the final destination of the goods, are obliged to register if they deliver goods to a person that does not have a tax identification number and the value of the goods exceeds CZK 1,140,000 without VAT.

Registration of other entities

The obligation to register as a VAT-taxable person also applies to entities that are not a VAT-taxable person but do engage in economic activities, including government bodies, national funds, municipal and other autonomous governing bodies, and other legal entities and persons that do not engage in entrepreneurial activities if the value of the goods acquired by them in the Czech Republic from another member state exceeds CZK 326,000,000 per calendar year.

VAT legal obligations

A VAT-taxable person is obliged to file a tax return for VAT and to pay the due tax within 25 days after the last day of the tax period. The tax period is generally one calendar month. However, if during the preceding calendar year the turnover of the VAT-taxable person did not exceed CZK 10,000,000, the tax period is a calendar quarter (i.e. three months).

The taxable period is always the calendar quarter for entities that do not have their seat, place of business or establishment in the Czech Republic.

A comprehensive report on intra-community deliveries of goods must be filed within 30 days after the end of the calendar quarter.

Deduction of tax on purchases

Tax can be deducted from purchases if the purchased goods and services are used for carrying out economic activities.

A person subject to VAT has the right to claim VAT for incoming (purchased) taxable supplies if he/she uses these for the purpose of performance:

- For supplies subject to tax; or
- For taxable supplies exempt from tax with the right to a deduction (e.g. delivery of goods to a member state, export of goods, providing a service to a third country).

The claim has to be proven by a tax document issued by a VAT-taxable person.

The right to a deduction may be claimed no sooner than during the tax period in which the taxable supply took place.

The right to deduct tax on purchases cannot be claimed for the purchase of personal automobiles (with the exception of automobiles purchased by a VAT-taxable person whose authorised business activity is the purchase of automobiles for their resale, including the purchase of automobiles through leasing agreements with the option of selling), or in the case of expenses for representation.

However, a VAT-taxable person does not have the right to deduct tax on purchases if he/she uses the performed supplies solely for supplies exempt from tax without the right to a deduction.

Services that are exempt from VAT are specified in the VAT Act as exempt, without the right to a deduction. These include financial services; insurance; postal services; radio and television broadcasting; the transfer and lease of real estate; education and training; medical and social care; services provided to members; services related to sports or physical education; services related to culture; the sale of postage stamps and stamped stationery; the operation of lotteries and similar games; sale of goods on the acquisition of which there was no right to a deduction of tax; and the collection of funds used for the activities of persons that have fulfilled conditions set out by the law.

Certain real estate transactions, specifically leasing, may be taxed, if the provider wishes, if the taxable supply is intended for a VAT-taxable person.

If the VAT-taxable person uses the performed supplies, for the exempt supplies as well as for taxable supplies, the right to tax deduction on purchases is limited by a quotient that is calculated as the proportion of

the taxable supplies with the right to a deduction of VAT to all taxable supplies.

If the VAT-taxable person claimed a deduction of VAT (in full or partially) for acquired long-term assets and a change in the right to the deduction occurs during the subsequent five calendar years as a result of a change in the purpose of the use of these assets, the VAT-taxable person must recalculate the amount of the right to a deduction and apply VAT to any difference there may be.

Export of goods is VAT exempt if the dispatch or transport of such goods is affected by their exporter and the buyer has no seat, place of business or permanent establishment in the Czech Republic.

A supply of goods to another EU member state is VAT exempt if such goods are dispatched or transported from the Czech Republic and the buyer is a VAT payer in another EU country.

In case of providing services to foreign person or person registered for VAT in another Member State, the place of fulfilment is transferred to the country of receiver, i.e. reverse-charge principle (for instance assignment of copyrights, advertising services, consultancy, financial services, rent of movable assets except for cars). These services are not objects of the Czech VAT.

Advance payments

Advance payments are subject to VAT during the period in which they are received. A company that receives an advance payment is obliged to issue a tax document (invoice), and must pay the relevant VAT on the amount and for the relevant period.

A tax document does not need to be issued in the following cases:

- An advance payment was received under a lease agreement;
- An advance payment was received under an agreement on the supply of energy, gas, or water; or
- A final invoice is issued in the same tax period (month) in which the advance payment was received.

A subject whose bookkeeping is not kept according to Czech regulations (e.g. physical person keeping only tax records) is exempt from the liability to pay advance payment from received payments. This subject can not issue the confirmations of received advance payments.

The following cases are subject to VAT:

- The delivery of goods and services in the Czech Republic;
- The import of goods from a third-party country by any entity;

- The procurement of goods from another member state (intra-community supplies); or
- The procurement of selected services ('reverse-charge') from other EU member states.

Non-monetary investments of assets to a business company or co-operative are also considered to be taxable supplies, with the exception of contributions consisting of a business or a part, which generally are not subject to VAT.

Real estate and VAT

The transfer of buildings, apartments and non-residential premises is exempt from VAT only after three years have passed from the date of acquisition or the date of an occupancy permit. The transfer of land is exempt from VAT, with the exception of 'construction land', which the VAT Act defines precisely.

The construction of apartments is subject to the reduced rate of 5%, and the construction of non-residential premises is subject to the basic rate of 19%.

VAT refunds

Foreign companies can receive refunds of VAT paid in the Czech Republic. The rules for the refund of VAT are set out in the provisions of the 8th and 13th EU Directives. VAT is refunded through a request filed by the foreign entity. Requests must be made on a separate application form in the Czech language and filed with the Tax Office for Prague 1 by 30th June of the year after the year in which VAT was applied for the delivery of the goods/services, or in which the VAT was paid for an import. The request must include the original invoices, the original documents issued for an import, as well as a list of the relevant invoices including a certificate of VAT registration in the country in which the entity making the request has its registered office or place of permanent residence.

Foreign entities must file a request for the refund of VAT within six months of the end of the calendar year for which the refund of VAT is being requested. A request may be filed only if the total of the Czech VAT exceeds CZK 1,000 for the given calendar year. Foreign entities may also file a request for the refund of VAT before the end of the calendar year for a period shorter than the calendar year; however, this request must be for a period of at least three calendar years and the total of the VAT paid during this period must be more than CZK 7,000. VAT is refunded by the Tax Office for Prague 1 within six months of the date on which the request was filed.

Conditions for a claim:

- A foreign entity is identified for the purposes of VAT in the country in which the entity has its registered office, base, or branch office;
- A foreign entity does not have its registered office, branch office or base in the Czech Republic during the period for which the request for the refund of VAT is being filed; or
- During this period the foreign entity does not sell goods and does not provide services in the Czech Republic, with the exception of: international transport and related auxiliary services; delivery of goods including assembly, if the customer is an entity that is subject to the tax.

VAT paid for the provision of services exempt from VAT cannot be claimed.

The tax office also has the right to reject a request for a VAT refund if the country in which the foreign entity is registered does not have a reciprocal treaty with the Czech Republic on refunding VAT.

Intrastat

The Intrastat system has been fully applied since 1 May 2004. As part of this system, VAT-taxable persons that engage in intra-community transactions (sending/receiving goods to/from other EU member states) are obliged to keep records of these transactions.

A third party (agent) can be appointed to keep records within the Intrastat system, but the obligation to keep records nevertheless remains the responsibility of the VAT-taxable person.

Excise tax

This tax applies to the consumption of five specified groups of goods: hydrocarbon and combustible substances and lubricants, alcohol, and alcoholic beverages, wine, beer, cigarettes and tobacco products. The tax is paid by the manufacturer or importer of these goods.

Excise tax is set as a fixed amount per unit of goods.

Contributions for General Health Insurance and Social Security of Self-Employed Persons

Self-employed persons are obliged to pay general health insurance contributions and social security contributions. The obligation to pay general health insurance contributions arises on the date when independent profit-making activities start.

Persons carrying out *primary independent profit-making activities* are always subject to the obligation to pay social security contributions, and those carrying out secondary *independent profit-making activity* are subject to this obligation if the income from the secondary independent profit-making activity after the deduction of related expenses reaches at least the decisive amount. If a person carrying out a secondary independent profit-making activity does not attain the decisive amount, the person can voluntarily apply for participation in social security.

The 'decisive amount' is 2.4 times the product of the general basis of assessment for the calendar year two years before the calendar year for which participation in the insurance is being assessed, and of the conversion quotient for the modification of the general basis of assessment.

The decisive amount for 2007 was CZK 45,200 (USD 2,165).

Independent profit-making activities are considered to be 'primary' if the conditions for 'secondary' independent profit-making activities are not fulfilled. Independent profit-making activities are a secondary activity if:

- The person is, in addition to the independent profit-making activity, also employed and the income from employment is at least 12 times the minimum wage;
- The person also receives an old-age pension or disability benefits; or
- The person is an un-provided-for child/student, etc.

The basis of assessment (annual) for mandatory general health insurance contributions and social security contributions is a percentage of the profit (the difference between income and expenses of the independent profit-making activity), as shown in the following table:

Basis of assessment for self-employed persons = % of profit	
In 2005	From 2006
45%	50%

There is a common maximum limit of CZK 486,000,000 (USD 20,900) for the basis of assessment (annual) for the calculation of general health insurance contributions and social security contributions, as well as a minimum limit that is different for general health insurance contributions and different for social security contributions (see below).

Minimum basis of assessment

General Health Insurance contributions

The minimum basis of assessment is 12 times 50% of the average monthly wage in the national economy for the calendar year two years before the year for which the basis of assessment is calculated.

The minimum basis of assessment for the year 2007 was CZK 120,834 (USD 5,800).

The minimum basis of assessment does not apply to persons on behalf of which the state pays contributions (un-provided-for children/students, senior citizens, women on maternity leave and parental leave, persons registered with employment offices, etc.), nor does it apply to persons who at the same time are employed and contributions are being paid on their behalf under this employment at least from the minimum basis of assessment calculated for the employee. If the independent profit-making activity is not carried out during the entire year, or if for part of the year the self-employed person receives sick-leave benefits from sick-leave insurance for self-employed persons, the minimum basis of assessment is reduced proportionately.

Social security contributions

The minimum basis of assessment (annual) for primary independent profit-making activities is 12 times 45% in 2005 and 50% from 2006 on the amount that is calculated as the product of half the general basis of assessment for the calendar year two years before the calendar year for which the basis of assessment is calculated, and of the conversion quotient for the modification of this general basis of assessment.

The minimum basis of assessment (annual) for primary activities in the year 2007 was CZK 56.508 (USD 2.707).

The minimum basis of assessment (annual) for secondary independent profit-making activities is 12 times 10% of the amount calculated as the product of the general basis of assessment for the calendar year two years before the calendar year for which the basis of assessment is being determined, and of the conversion quotient for the modification of this general basis of assessment.

The minimum basis of assessment (annual) for secondary activities in the year 2007 was CZK 22.608 (USD 1.083).

If primary or secondary independent profit-making activity is carried out for only part of the calendar year, the minimum basis of assessment is reduced proportionately.

Contribution rates

Self-employed persons – contribution rates for:		
General health insurance	Social security *	Sick-leave insurance – voluntary
13.5 %	29.6 %	4.4 %

* Includes pension insurance contributions and unemployment benefit contributions.

A self-employed person is not obliged to pay contributions for sick-leave insurance; however, a self-employed person can apply voluntarily. A self-employed person can participate in sick-leave insurance only from the day on which the person filed the relevant application. Contributions for sick-leave insurance are calculated from the monthly basis of assessment, unlike contributions for social security and general health insurance, where an annual basis of assessment is calculated and monthly advance payments are determined on the basis of the economic results of the self-employed person during the previous year.

7. Accounting & reporting

Accounting is governed by the Accounting Act and related regulations (decrees on accounting and Czech accounting standards). There have also been changes in regulations on accounting as a result of the admission of the Czech Republic to the EU.

Persons registered in the Commercial Register (including organisation sections) as well as natural persons that engage in business and have a turnover of more than CZK 15,000,000, must keep accounts in the Czech language. The accounting period can be the calendar year, or a business year that differs from the calendar year. Accounts must be kept in the Czech currency; in addition, receivables, liabilities, shares, securities, and cash or accounts in foreign currencies must also be stated in a foreign currency.

Chart of accounts

Each accounting unit must prepare a mandatory chart of accounts, i.e. an overview of the accounts that it uses. The mandatory basic structure of a chart of accounts is set out in decrees on accounting for the various types of accounting units (entrepreneurs, non-entrepreneurial entities, banks, insurance companies, government organisation sections); a detailed breakdown of the chart of accounts into general accounts and a further more detailed breakdown of analytical accounts are determined by the accounting unit according to its needs.

Basic structure of a chart of accounts for entrepreneurs:

Class	Description
0	Long-term assets (tangible assets, intangible assets, financial investments, accumulated depreciation on assets)
1	Inventory (supplies, products, goods)
2	Short-term financial assets (cash, bank accounts, short-term loans, short-term securities)
3	Claims and liabilities (receivables, obligations, advance payments to business partners, employees, government institutions)
4	Equity capital and long-term liabilities
5	Expenses
6	Income
7	Closing accounts and off-balance-sheet accounts

Closing of books

As of the balance date, entrepreneurs submit a financial statement – a balance sheet, a profit and loss report, and an appendix. The appendix contains supplementary information on the balance sheet and profit and loss report, and specifically contains information about the accounting methods used, a specification of the content of the entries in the balance sheet and profit and loss report, liabilities to the government, and can also contain a cash flow statement.

The financial statement is a required appendix of a tax return.

Companies are obliged to make public their annual reports, financial statements, and audits of financial statements by depositing them in the collection of documents with the registration court within the deadlines set by law.

Audit

The following three criteria are decisive in determining whether there is an obligation to conduct an audit:

- Net assets of more than CZK 40,000,000;
- Net turnover of more than CZK 80,000,000; or
- Average number of employees of more than 50.

Joint-stock companies are obliged to conduct an audit if at least one of the criteria is fulfilled in the year for which the closing of books is being prepared, and in the preceding year. For other business companies, co-operatives, organisation sections of foreign entities, and natural persons keeping double entry accounting, an audit is mandatory if at least two of the three conditions are fulfilled for two consecutive accounting periods. Audited companies must prepare an annual report.

International Accounting Standards

Since 2005, consolidating accounting units that issue securities registered on a regulated market in EU member states are obliged to use International Accounting Standards for financial statements. Other consolidating units have the choice of applying International Accounting Standards for their financial statements.

However, the application of International Accounting Standards does not affect the assessment of taxes because legal entity income tax must be calculated in accordance with Czech accounting and tax regulations.

8. UHY firms in the Czech Republic

AUDITOR, spol. s r. o.
Haštalská 6
110 00 Prague 1
Czech Republic

Contact: Georg Stöger
Tel: +420 224 800 411
Fax: +420 222 326 634
Email: praha@auditor-eu.com
Web: www.auditor-eu.com

With offices also in: Pelhřimov

For more details, please visit: www.auditor-eu.com

9. UHY offices worldwide

For contact details of UHY offices worldwide, or for details on how to contact the UHY executive office, please visit www.uhy.com