



Tax reform

In its resolution dated 2 April 2007 the government presented its draft tax reform, which is intended to amend 6 tax laws to come into effect in principle on 1 Jan 2008. However, the draft amendment is still to be discussed in Parliament and then in the Senate of the Czech Republic, and it is quite uncertain whether it will be approved. Below we present a summary of some of the proposed changes.

■ Income tax

The income tax law is to be changed significantly by introducing a uniform rate of 15% for the income tax of natural persons and by the gradual reduction of corporate income tax from the current 24% down to 19%. However, the tax rate reduction is to be compensated through changes in the way in which the tax base is determined. Consequently, there will be no significant reduction in the tax burden.

As for the income tax of a natural person, the manner of determining the tax base for income from dependant activity is to be changed: the tax base cannot be reduced by premiums paid by employees for health insurance and social security; on the contrary, the employee's tax base will consist of the gross wage of the employee increased by employer's contribution for health and social insurance. Self-employed natural persons will be limited to a lump-sum upper limit of CZK 1,500,000 per tax period for the application of expenses for tax purposes.

The joint taxation of married couples is to be abolished; however, at the same time discounts from the natural person tax are to be increased. For example, the existing basic discount for a taxpayer will grow from CZK 7,200 to CZK 24,840; the discount for a wife without her own income is to be increased from CZK 4,200 to 24,840.

Among the proposed changes is new relief for a natural person income from the sale of securities, income from the sale of ownership interests (participation shares) in trading companies or membership rights in a co-operative, if a determined time of the holding of securities or ownership interest is met. An exemption should be possible only in cases of the transfer of membership rights in a housing co-operative, if the sale is realised no sooner than 5 years following acquisition.

For legal entities, rules for tax deductible costs are to be stricter. For example:

Costs spent by the employer for employee meals, e.g. in the form of meal vouchers, are not to be tax assessable costs of the employer.

Conditions for the tax deductibility of interest on credit and loans from affiliated persons are also to be stricter. Tax deductibility of costs for financing provided from not affiliated persons is now to be limited, if such financing exceeds a six-fold of equity. Also, the total cost for financing that which could be tax deductible is also to be limited to 6% of the average size of the actually used credit and loans.

The tax base is to be increased by the unpaid liabilities of taxpayers which are overdue for 36 months or which are time barred.

The tangible assets subject to depreciation pursuant to the income tax law will be assets of CZK 20,000 and over, whereas the lower limit for intangible assets will be CZK 40,000. Conditions for the tax deductibility of costs related to financial leasing are also to be stricter.

Some conditions for the creation of adjustable items to receivables are also to be changed by the new legislation.

■ Value added tax

The reduced tax rate is to be increased from the current 5% to 9%. The amendment includes also the already advised definition of "social housing", for which the reduced tax rate could also be applied after 2007. The "social housing" condition should be met by flats with a floor area of up to 120m² and by family houses with a total floor area up to 350m².



Taxpayers could now ask for a binding assessment of the tax rate.

From 2010 on, taxpayers with an obligatory monthly tax period are to submit tax returns and summarised reports in electronic form only.

■ Real estate property tax

The amendment proposes to relieve from taxation land not burdening the municipal infrastructure (such as arable land, hop raising yards, vineyards, orchards and perennial grass surfaces).

Inheritance tax, donation tax and tax from the transfer of real estate

Full exemption from inheritance and donation taxes is to be relevant not only for the acquisition of property from relatives in direct lineage and from a marital partner, but also for acquisitions from other relatives.

■ Excise taxes

The amendments include in particular a change of taxation for waste oils and an increase in tax on cigarettes so as to reach the minimum rate set in the European Union.

The law on registration cash-desks is to be cancelled without any substitute legislation.

■ Instruction D – 300

On 1 January 2007 the new instruction D-300 came into effect, which replaces the original instruction D-190 and which provides explanations to some provisions of Act No. 586/1992 Coll. on income taxes. Instruction D-300 should essentially be an up-date of the original instruction D-190; hence, it deals with many amendments to the income tax law as well other laws (e.g. law on value added tax). At the same time, it includes some explanations of the law approved by the Czech Ministry of Finance in the so-called co-ordination boards with representatives from among tax advisors.

The instruction is not binding upon taxpayers. However it should be binding for employees at financial offices (Inland Revenue Authorities), which should follow the instruction in their application of the income tax law. The instruction should provide more detailed information to the interpretation of the law. However, the interpretation should not exceed the framework of the law; i.e. it cannot impose obligations or provide rights not stipulated by the law. Below is a summary of some of the changes from instruction D-190.

Exemption from the payment of dividends and shares on profit

- the minimum holding for exemption of profit from taxation has to be met on the date when the general meeting is held
- the exemption does not relate to profits decided upon by the general meeting after a subsidiary has entered liquidation, except for payment of a subsidiary to the parent company from another member country
- the exemption can also be applied to interest not deductible as expense for low capitalisation and to the unacknowledged difference between an agreed price and a usual price (re-classified to shares on profit)

Re the tax non-deductible costs related to the holding of interest/shares in a subsidiary

- costs for the execution of the competence of a general meeting of a subsidiary by the parent company are for example:
 - other costs for the application of shareholder's rights
 - costs connected with the participation of a parent company's employee who is at the same time a body or member of bodies of the subsidiary at the meetings of such bodies or at a general meeting of the subsidiary
 - costs for the participation of a person authorised to act on behalf of a shareholder/partner – the parent company – at a general meeting of the subsidiary
- the instruction further provides examples of direct and indirect costs related to the



- holding of participation shares/ownership interests
- expenditures of the parent company related to the holding of a share in the subsidiary are not subject to taxation only for the time of holding the participation share (ownership interest) (on changes up to the record day).

Tax deductible costs

- with expenditures specified in Section 24 subsection (2) of the Income Tax Law no link to tax deductible income is necessary
- the instruction defines a so-called "record day" for the inclusion of some amounts in the tax base:
 - the date when a court decision comes into legal force
 - the date of a complaint procedure ends
 - the date on which a legal entitlement to a discount or a bonus arises
 - withdrawal from a contract, the date the contract is cancelled
 - the date of a settlement agreement
 - the date on which an absolutely invalid legal act was originally made
 - the date an additional payment assessment was delivered
- exchange rate differences are always part of the tax base (both realised and unrealised) regardless of whether they relate to tax or non-tax expenses or income
- tax on real estate transfer paid by the guarantor for the original owner is a tax expense for the guarantor also in such a case when it was paid before the owner was invited to do so by the tax administrator
- the following are also tax expenses:
 - additionally assessed road tax, value added tax and excise tax, if they relate to tax expenses,
 - value added tax due to incorrectly paid tax on output,
 - real estate tax and tax on the transfer of real estate, if already paid
- compensation for failure to meet the statutory registration obligation pursuant to Section 98 of the Act No. 235/2004 Coll. on value added tax is also a tax expense
- business trips include also trips of statutory bodies made in connection with the execution of such posts, if meetings are held at a place other than in the registered office of the company

Technical valuation

- the term "technical valuation" does not include the mere substitution of the material applied, also in the case of the replacement of windows with wooden frames for windows with plastic frames, if the original dimensions of the windows and the number of glass layers of windows are preserved. Fitting a motor vehicle with winter tyres is not a "technical valuation".

Tax losses

- application of losses during 5 (7) tax periods
 - the loss can also be applied in periods which are not tax periods, but for which tax returns are submitted
 - such periods are not included in the number of 5 (7) periods for the application of losses
- the instruction includes a detailed explanation of the application of the law, which is restricted under certain conditions to the tax deductibility of losses (e.g. for changes in the structure of partners or in cases of transformations)

Tax on the income of natural persons

- for an employee to which an option for the purchase of shares was provided gratuitously, the taxable income from dependable activity shall only arise at the moment when the option is used i.e. not at the moment when the option is granted



- for the purposes of the exemption of non-monetary income from the income tax of natural persons, the instruction now omits the condition that the work clothes and shoes must not be of a shape, colour etc. that could be confused with normal civil or social clothing
- the condition of transient accommodation for the purposes of claiming exemptions on non-monetary income if such accommodation is provided to an employee from abroad shall not be met unless the transient accommodation for the employee from abroad is a permanent flat (apartment), in which such employee will permanently stay within the meaning of the "permanent flat" for purposes of obtaining tax residence in the Czech Republic.

■ Digitalisation of the Companies Register

Since 1 Jan. 2007 the entrepreneurs (business entities) registered in the Companies Register are obliged to file certain documents with the Collection of Deeds (in Czech "Sbírka listin") only in electronic form. This does not apply to documents which are filed with the Collection of Deeds but which do not prove facts stated in a proposal for entry or change or cancellation of an entry/registration in the Companies Register, such as annual reports, financial statements and reports on relationships between interconnected persons. Such documents can be sent to the Registry Court via electronic mail or using a CD-R data carrier. The Registry Court does not return any delivered data carriers and will discard them 6 months following their delivery.

■ Customs declaration in electronic form

Based on the Order of the Council No. 1875/2006, which came into effect in principle as of 1 Jan 2007, the export customs declaration can only be filed as of 1 July 2009 in electronic form with the exception of defects in the systems of the customs authorities or of the exporter. The individual membership countries were gradually joining the project of electronic imports when the Czech Republic commenced its electronic export as early as on 1 Feb 2007. Although the customs authorities will probably already require electronic filing, they cannot impose the obligation of electronic filing before 1 July 2009 with regard to the date of the aforementioned order.

For the purposes of electronic filing an electronic signature is mandatory. Pursuant to Section 30 of the Act on VAT, a document is a declaration with electronic signature filed in electronic form. As some countries have not already introduced the electronic export, there could be problems with the confirmation of exit of the goods from the EC territory in the transient period (i.e. till 1 July 2009). Therefore, the procedure will be the same as up to the present in some cases, which means that the taxpayer's document will be confirmed by the customs authority on exit. In the case of electronic filing, it is the Export Accompanying Document. Alternatively the taxpayer will have to prove the export of goods from the EU in another manner.

■ Sending Intrastat via Internet in electronic form

Intrastat statements can now be sent by means of the InstatOnline web application, which is available on web sites of the customs office at www.cs.mfcr.cz. For entry, it is necessary to register at the locally competent customs office and fill out a request for permission to use electronic communication.

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