



Investment in the Czech Republic

Meet the Heart of Europe

2016





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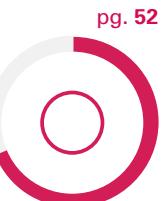
Corporate
transactions



Financial
services



How
KPMG can
help



Direct
taxes



Useful
addresses

... and more



Welcome to the Czech Republic

In today's highly competitive and dynamic economic environment, few decisions are as critical to success as selecting your business location. Most entrepreneurs at some point consider **relocating to create fresh momentum and pursue new growth opportunities**.

Compared to its regional peers, the Czech Republic is doing fairly well in terms of GDP per capita and in terms of competitiveness. It also clearly stands out as a regional champion in the inflow of FDI. Currently, the Czech Republic is experiencing growth across various sectors of the economy, including **merger and acquisition activity**.

While cost is a factor, it is only one of many considerations that influence the choice of destination: an education system that yields a highly skilled workforce; high living standards and a diverse culture; capacity for innovation; a modern infrastructure combined with a position in the heart of Europe.

The Czech Republic has been a popular destination for foreign capital and has attracted high volumes of foreign direct investment (FDI) since the 1990s. FDI activities in the Czech Republic stand out in a very important feature: profitability.

The Czech Republic is home to **many advantageous conditions** – from its geographical location combined with a reliable infrastructure, availability of suppliers and specialized inputs needed by foreign investors, to quality of life and social stability, cost competitiveness, financial stability and availability of financing, investment incentives as well as a skilled workforce and a high educational level, all making it an attractive location for all types of investors and companies.

This publication sets out insights and data relevant to **planning investments or conducting business** in the Czech Republic. As the tax and legal systems in the Czech Republic are still comparatively new, certainty about the legal

effects of transactions is sometimes less easy to obtain than in more developed economies. In addition, Czech and EU legislation are frequently amended. Accordingly, the information should be viewed only as a general guide for preliminary planning purposes.

I nevertheless hope it will be a helpful source of **background information and a constructive tool** in making your investment decisions.

Combining KPMG's insights and expertise in relocation issues, we can help you determine if the Czech Republic is the right base for your business in Europe. If you have any questions, remarks or suggestions, please feel free to contact the respective KPMG experts.

We look forward to assisting you with your investment in the Czech Republic.

Jan Žurek,
Managing Partner,
KPMG in the Czech Republic





Meet a regional champion

Where the Czechs score the best. The Czech Republic clearly stands out as a regional champion for the inflow of the foreign direct investments. Among the new member states of the EU¹ the Czech Republic is:

#1



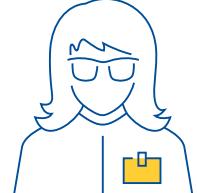
— in quality of air transport

#1



— in country capacity to retain and attract talent

#1



— in company spending on R & D (Research and Development)

#1



— low wastefulness of government spending

#1

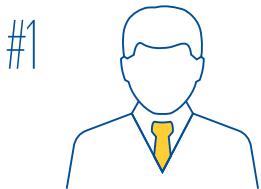


— in quality of electricity supply

#1



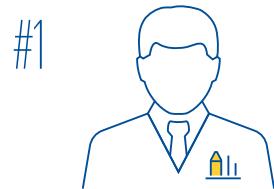
— in soundness of banks



— in trustworthiness
and confidence



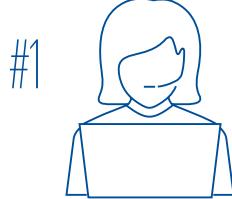
— in state of cluster
development



— in capacity for
innovation



— in local supplier
quality



— in business
sophistication



— among the competition of
10 new member states of the EU

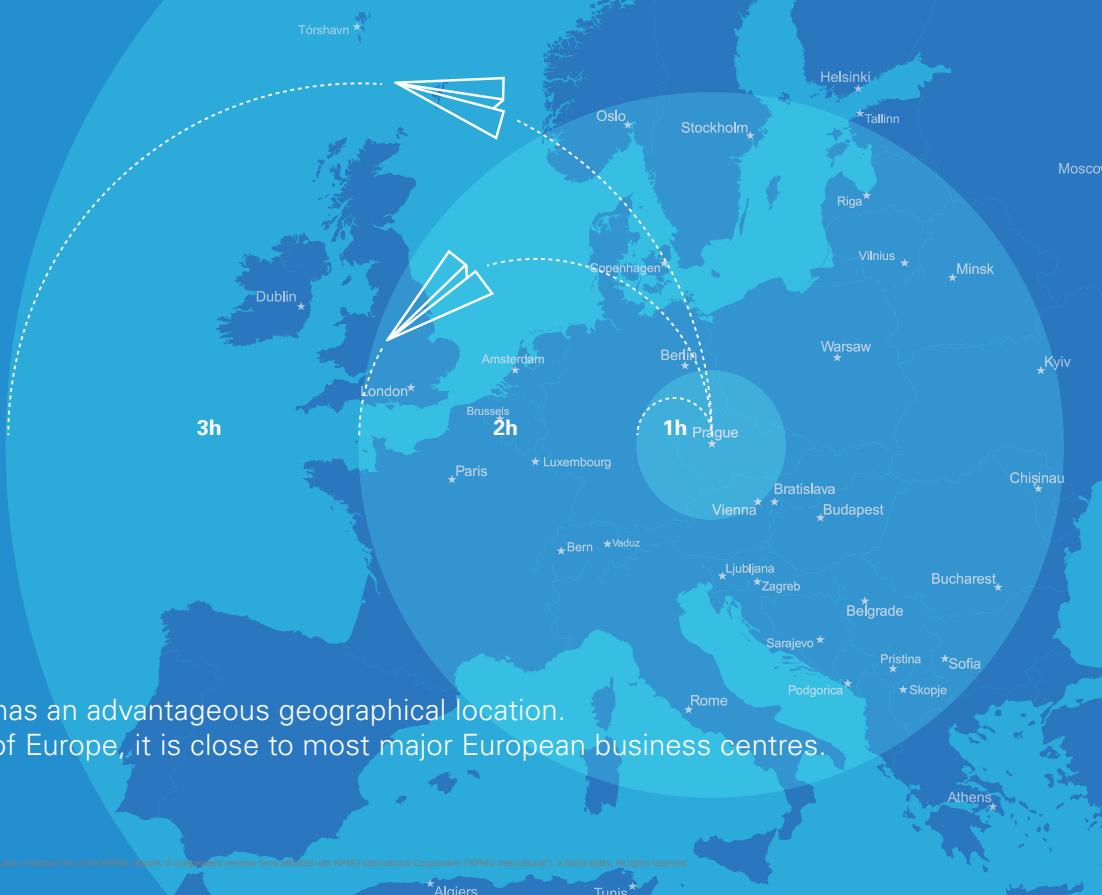
In the overall Global Competitiveness Report 2015-2016², the Czech Republic ranks 31st in the competition of 144 countries in the world. It has made remarkable progress **from 37th to 31st place** since 2014-2015.

1 Central and Eastern European new member states of the EU; this group consists of 10 post-socialist countries which entered the EU in 2004 and 2007: Bulgaria, Czech Republic, Estonia, Latvia, Lithuania, Hungary, Poland, Romania, Slovakia and Slovenia.

2 The Global Competitiveness Report 2015-2016 assesses the competitiveness landscape of 144 economies, providing insight into the drivers of their productivity and prosperity. The Report series remains the most comprehensive assessment of national competitiveness worldwide.



Meet your business destination in the geographical heart of Europe



Meet a popular foreign capital destination

The Czech Republic is one of the most successful CEE countries in terms of attracting foreign direct investment (FDI) since the 1990s. Where did most of the FDIs originate?



The primary investment sectors are:

- manufacturing
- financial institutions
- real estate
- transport and communications

Investment incentives include:

- systematic investment incentives schemes
- tax breaks for up to 10 years
- subsidies related to job creation and employee training
- support related to the acquisition of land

The Czech Republic has been given **a strong vote of confidence** from investors with first-hand experience of the Czech economic environment.



Meet your investment opportunities

Automotive¹

Globally, the Czech Republic is the second largest passenger car producer per 1 million inhabitants.

The Czech Republic hosts one of the highest concentrations of automotive manufacturing enterprises. By volume alone, it belongs to the 15 largest global passenger car producers. It has a long industrial tradition and is able to compete at a global level. More than half of the world's top-100 tier one suppliers are located in the Czech Republic.

Current successful investors:

**Hyundai, Johnson Controls, Volkswagen/
Škoda Auto, Bosch, Toyota/PSA, Valeo**



Aerospace¹

Prague, the capital of the Czech Republic, is home to the headquarters of the European Global Navigation Satellite Systems Agency.

A strong engineering background, excellent research and development (R&D) facilities, an outstanding product reputation and high product reliability ensure safe investment opportunities. The Czech Republic is an active member of the European Space Agency.

Current successful investors:

Honeywell Aerospace, GE Aviation, Latecoere



Business support services¹

The Czech Republic offers business support services in financial, accounting, IT, customer support, human resources, purchasing, logistics and legal services.

What makes the Czech Republic one of world's most attractive locations for business? The answer is simple: its location, infrastructure and a skilled workforce with foreign language skills.

Current successful investors:

DHL, Accenture, SAP, Infosys

Energy and the environment¹

The Czech Republic offers abundant opportunities for investors in the design, manufacture and delivery of new technologies for environmental protection and energy savings.

When investing in the Czech Republic, you can count on top technical competence, manufacturing excellence and cost effectiveness.

Current successful investors:

Doosan, Vyncke, Solar Turbines, Bilfinger



High-tech mechanical engineering¹

The Czech Republic is home to world-class mechanical engineers. Over 80 % of the sector's output is exported.

The sector's main exports are turbines, transportation solutions, air-conditioning equipment, construction machinery and machine tools.

Current successful investors:

Ingersoll Rand, Siemens, Edwards, Daikin

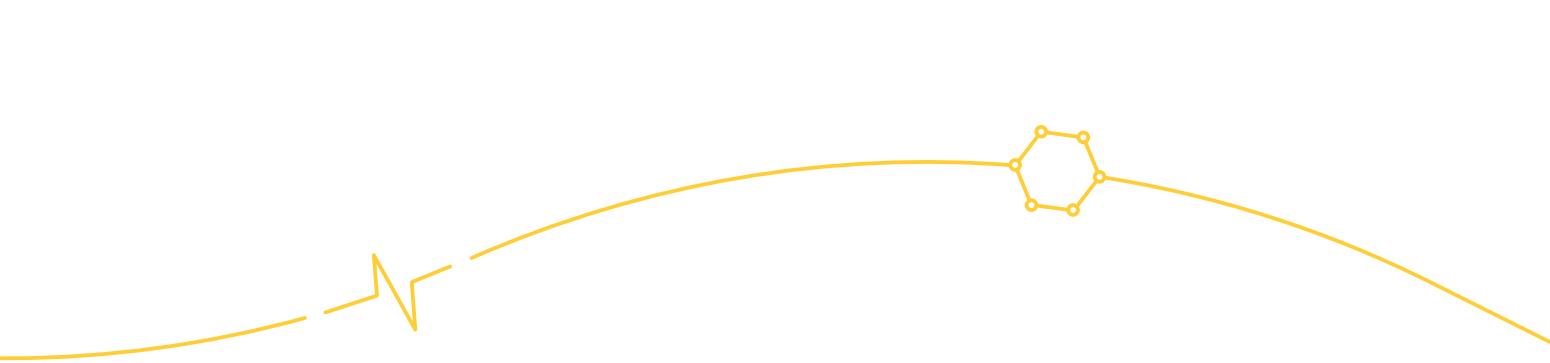
Information and communication technologies¹

The Czech Republic represents one of Europe's top locations for ICT investments, outsourcing and offshoring IT-related services and software design.

With the Czech Republic's strong inflow of high value-added projects, tradition of excellence in technical fields and heritage of thorough technical and mathematical education, the Czech origins of global ICT companies like AVG Technologies, AVAST and Y Soft are not surprising.

Current successful investors:

Microsoft, Skype, NetSuite, Tieto, Red Hat, SolarWinds and IBM



Life sciences¹

Viread, a successful antiviral drug for the treatment of HIV/AIDS has been developed at the Czech Academy of Science's Institute of Organic Chemistry and Biochemistry.

The country offers a growing network of research clusters, state-of-the-art research facilities, attractive locations for manufacturing and contract R&D operations plus effective patent protection. The government's policy goals include the continuation of R&D support. GMP, GLP and GCP standards have been adopted.

Current successful investors:

Sanofi, TEVA, Lonza, Otsuka



Nanotechnologies and materials¹

The Czech Republic is proud of its network of collaborating business companies which has emerged around top research institutions involved in the most prestigious projects.

CEITEC, the Regional Centre of Advanced Technologies and Materials, the Technical University of Liberec are undisputedly world-class centres of nanotechnology research. They are supported by a state-of-the-art research infrastructure and by the Czech Nanotechnology Cluster and Nanotechnology for Society funding programme.

Current successful investors:

Microsoft, Skype, NetSuite, Tieto, Red Hat, SolarWinds and IBM

¹ Investment Climate in the Czech Republic, 2015, CzechInvest



The current macroeconomic forecast

Main macroeconomic indicators:
Current macroeconomic forecast 2016¹

Gross domestic product bil. CZK **4 657**

Average inflation rate % **0,5**

Unemployment rate (LFS) average in % **4,7**

Current account balance % of GDP **1,2**

Exchange rate CZK/EUR **27,0**

Long-term interest rates % p.a. **0,7**

The Czech Republic is a country with relatively low external and internal macroeconomic imbalances and manageable levels of public debt and deficits. **A stable and healthy banking sector** with excess liquidity is able to meet the financing needs of both domestic and foreign investors with **a minimal risk of losses** due to financial crises and related instabilities.

¹ <http://www.mfcr.cz/en/statistics/macroeconomic-forecast/2016/macroeconomic-forecast-january-2016-23829>

(Winter 2015 estimates)

European Economic Forecast ² :	2016	2017
GDP growth	2,3%	2,7%
Inflation to remain below	0,4%	1,4%
Unemployment rate to decline moderately	from 4,8%	to 4,7%
Public budget deficit to decline	from -1,1% of GDP	to -1,0% of GDP
Indebtedness of the general government sector (gross public debt) to decrease	from an estimated 40,7 % of GDP	to 40,1% of GDP

2 http://ec.europa.eu/economy_finance/eu/countries/czech_republic_en.htm

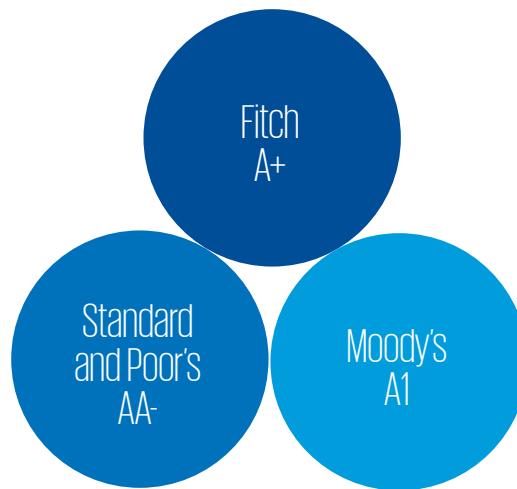
In the European Economic Forecast, the Czech Republic is praised for its progress:

- in increasing growth-enhancing expenditures;
- strengthening the fiscal framework;
- developing public employment services;
- in improving tax compliance, pension and healthcare reform;
- in enhancing the inclusiveness and quality of education;
- in reforming regulated professions and public administration;
- public debt below the 60% of GDP threshold.



Ratings

The Czech Republic has been rated very positively by all three major rating agencies, i.e. Moody's, Standard and Poor's and Fitch.



Foreign currency long-term sovereign debt ratings
(www.cnb.cz); Last update: 1st October 2015



The Czech Republic in numbers

The Czech Republic is an advanced democracy with a free-market economy. It is well known for its skilled workforce, reliable infrastructure, cost competitiveness and high educational level. Favourable labour costs are also among the main attractions of the Czech economy.

Prague, the capital as well as the largest city with a population of **1.2 million**, other major urban centres:

- **Brno** (376,822)
- **Ostrava** (294,955)
- **Plzeň** (168,377)
- **Liberec** (102,405)
- **Olomouc** (99,555)
- **Ústí nad Labem** (93,536)
- **České Budějovice** (93,175)
- **Hradec Králové** (92,871)
- **Pardubice** (89,530)

- **Since 1989** a parliamentary republic with multi-party democratic political system
- **3 distinct regions**: Bohemia, Moravia and Silesia
- **10.5 million** = population
- **5.3 million** = a working population of about
- **78,864** square kilometres (30,500 square miles) = area
- **Since 1999** a member of NATO
- **Since 2004** a member of the EU
- **Since 2007** a member of Schengen



Living in the Czech Republic

Foreign nationals coming to the Czech Republic are subject to the so-called Foreigners' Act, which establishes two categories of foreigners: citizens of the EU, the EEA and Switzerland and nationals of third countries.

Residency and visas

To stay in the Czech Republic for more than three months, citizens of non-EU countries require a long-term visa or a long-term or permanent residence permit.

Natural persons with permanent residence outside the Czech Republic or legal entities with a registered office outside the Czech Republic may run a business in the Czech Republic under the same conditions and under the same limitations as a Czech person/entity.

Cost of living in Prague¹

Average prices of goods and services are 36.4 (including rent) compared to the New York benchmark of 100.



Wage levels are 20.3, compared to the New York's 100.

¹ Goods and services comparison is based on the cost of a basket of 122 goods and services weighted according to European consumption habits. <https://www.ubs.com/microsites/prices-earnings/edition-2015.html>. Wage levels are calculated as effective hourly wages for 15 professions, weighted by distribution; net after tax and social security deductions. UBS, Prices and Earnings (Edition 2015); at: <https://www.ubs.com/microsites/prices-earnings/edition-2015.html>



- The Czech healthcare system provides a high level of **professional medical care** assured by various health insurance providers. For foreigners, it is essential to have medical insurance to be able to pay for the cost of care.
- Numerous **international schools** exist in the Czech Republic, offering a growing choice of foreign-language educational programmes, ranging from preschools to MBA degrees.
- Prague and other larger Czech cities offer **international cultural institutes or clubs**, e.g. the American Center at the US Embassy in Prague or the Goethe Institut (www.goethe.de/ins/cz/pr).



***Lípa /li:pa/**
Small-leaved lime (linden)

The Czech national tree and symbol since 1848, designated as such during the First Pan-Slav Congress to counterbalance the pan-Germanic oak tree. A symbol of protection thanks to its attractive crown, lovely smell and inviting shade. About 1850 small-leaved limes have been given protected tree status in the Czech Republic.

Investment incentives and state aid

The Czech Republic's current attitude towards incoming investors is the most positive in its history.

Attracting new investment

Over the past few years, the Czech Republic has significantly increased its focus on both green field investments and the expansion of existing investments.

It currently has the most positive attitude to incoming investors in its history.

Investors can obtain the following financial benefits:

- investment incentives – tax holiday + cash grants;
- subsidies from EU funds – cash grants;
- R&D tax allowances;
- education tax allowances.

All benefits are provided according to the law and transparency rules, which are in compliance with EU regulations. In this respect, some measures have been redesigned further to a change of EU rules in 2014. EU regulations have generally become stricter and to a certain extent limit the granting of incentives by individual member states. The Czech government responded to the new rules with an amendment to the Czech Act on Investment Incentives, effective since May 2015. **The aim of the last amendment is to increase the attractiveness of investment incentives for investors** and to reduce the impact of the new EU rules

on them. The information below is based on the new legislation.

Investment incentives

Forms of support

Incentives are provided in the following forms:

- corporate income tax relief for up to 10 years (tax holiday);
- employment subsidies in the form of cash grants for job creation and training (only available in regions with high unemployment rates);
- cash grants for strategic projects;
- availability of land at discounted prices;
- exemption from real estate tax in selected industrial zones.

Main conditions

The main conditions for granting investment incentives differ depending on the supported activity.

Manufacturing industry:

- establishment of a new manufacturing plant, or expansion of an existing plant, including its modernization and diversification of product portfolio;
- minimum investment in tangible and intangible assets of CZK 100 million

(approx. EUR 3.6 million or USD 4 million), in selected regions this is reduced to CZK 50 million. Machinery must be new;
— creation of at least 20 new jobs.

Technology centres:

- establishment of a new technology centre, or expansion of an existing technology centre;
- minimum investment in tangible and intangible assets of CZK 10 million (approx. EUR 360,000 or USD 400,000), of which at least CZK 5 million must be invested in machinery. Machinery must be new;
- creation of at least 20 new jobs.

Business support services centres:

establishment or expansion of:

- shared services centre
- software development centre
- high-tech repair centre
- customer support centre
- data centre;

creation of at least 20 new jobs for software development centres, 500 new jobs for customer support centre or 70 new jobs for other business support services centres.

The following conditions apply for all types of investments:

- The acquisition of assets for the project, including construction work,

cannot start before the application for incentives is submitted.

- The investment must be maintained (in the minimum amount and structure) for at least five years from its finalization.

Strategic investment (large projects)

- Large projects can qualify for strategic investment status.
- The main benefit of this status is the possibility to obtain a higher portion of incentives in cash instead of tax relief.
- Cash grants can reach up to 10% and can be further increased to 12.5% in case of projects combining manufacturing sites and technology centres.
- For strategic investments in the manufacturing industry, the minimum amount to be invested in fixed assets is CZK 500 million, of which CZK 250 million must be invested in new machinery. At least 500 jobs must be created.
- For strategic investments into technology centres, the minimum amount to be invested in fixed assets is CZK 200 million, of which CZK 100 million must be invested in new machinery. At least 100 jobs must be created.

Income tax relief

Calculation

The tax treatment of a new company (plant) differs from that of an expanded facility only in the calculation of tax relief that can be claimed. For new companies, taxpayers are entitled to full tax relief, excluding tax on net interest income.

For the expansion of an existing plant, the amount eligible for tax relief is the difference between the tax relief that would be available for a new company and the average of the tax liabilities in the three years immediately preceding the first year in which tax relief can be claimed. The latter figure is adjusted with reference to industrial inflation and the current tax rate. This formula represents a rough attempt to limit the amount eligible for tax relief to any additional profits resulting from the expansion.

Permissible level of state aid and subsidy amounts

The total value of incentives must not exceed the maximum permissible level of state aid. The maximum amount of state aid is based on the rules set by the EU and is set at 25 percent of eligible costs (investment in land, buildings, machinery and equipment and selected intan-

gible assets) except for Prague, where no incentives can be provided.

For technology centres and business support services centres, eligible costs may alternatively comprise the wage costs of employees in newly created jobs within 24 months of the month in which a particular position was filled.

Job creation

Cash grants will be provided to employers creating new jobs in regions with unemployment at more than 25 percent above the national average or in special economic zones. The cash grants may amount to CZK 100,000 – 300,000 per new job.

Training and retraining of employees

Cash grants for the training and retraining of employees will be provided to employers in the form of partial reimbursements of the costs incurred. Subsidies may cover 25 percent of the eligible costs of employee training and retraining.

Purchase of construction sites

The actual provision of this incentive depends on negotiations with the owner of the land (state, region or municipality). The difference

between the market price and the actual purchase price is treated as an incentive.

How can KPMG help investors in the area of incentives?

KPMG in the Czech Republic is a leading advisor on investment incentives and can help investors with:

- initial assessment of whether their project qualifies for investment incentives;
- calculation of estimated benefits;
- preparation of applications for investment incentives;
- full support during the approval process;
- full support during the implementation phase;
- negotiations with the government on extraordinary incentives;
- site selection analysis.

To obtain more detailed information, please contact Jan Linhart at jlinhart@kpmg.cz.

EU structural funds

The Czech Republic (excluding Prague)

Businesses set up in the Czech Republic can also obtain support from EU Structural Funds under several operational programmes.

EU funds are available mostly in form of investment cash grants. A wide selection of grants is available. **The grants below are the most relevant to new investors:**

- Programme Innovation – support for innovations in production;
- Programme ICT – shared service centres;
- Programme Potential – support for R&D centre expansion/establishment;
- Programme Energy Savings;
- Program Applications – support for operational costs of R&D projects.

The first round of calls (i.e. periods for projects application submission) has already finished. A second round is planned for summer 2016. To obtain more detailed information, please contact Jan Linhart at jlinhart@kpmg.cz.

R&D tax allowance

Companies performing R&D activities may apply a special tax deduction.

The R&D deduction in fact allows companies to claim internal R&D costs twice: first within the profit and loss account, second as a special tax deduction. Effectively, savings can thus be up to 19 percent of R&D costs. The deduction can be claimed every year and there is no limit on the maximum amount to be claimed.

KPMG in the Czech Republic is an authorised advisor in the area of R&D tax deductions and provides a wide range of related services. It can help clients with:

- eligible activity definition;
- calculation of the deduction;
- preparation of required documentation;
- obtaining a ruling from the tax authority;
- issuance of a certified court expert opinion.

Education tax deduction

The education tax deduction was introduced as a new tool in 2014. It allows companies to obtain a special tax deduction for certain costs relating to vocational or professional education activities.

The deduction covers various activities relating to the education of secondary school or university students on the premises of companies. Companies can also receive a deduction for assets acquired for the purposes of such education.





***Slivovice /slɪvəvɪtsɛ/**
Slivovitz, plum brandy

A distilled alcoholic beverage made of different types of plums. Traditional slivovice for home or small-scale consumption is produced in private distilleries and is very strong, with an alcohol volume of around 52%.

Business structures

Establishing a company in the Czech Republic is neither financially demanding nor very time-consuming – e. g. for a limited liability company (s. r. o.), minimum registered capital of CZK 1 is sufficient and the company can be established within one month.

The basic provisions governing business obligations and other specific aspects of doing business in the Czech Republic are set out in the Civil Code and the Act on Business Corporations, both effective as of 1 January 2014.

The Act on Business Corporations addresses the main aspects of Czech corporate law. It also regulates the relationship between companies and their statutory representatives, their rights, obligations and liabilities for breaches of due care. Further, it sets out the rules for holding companies and the liability for damage caused by their controlling entities.

Types of business entities

The Act on Business Corporations recognises the following types of business entities:

- limited liability companies;
- joint-stock companies;
- general partnerships;
- limited partnerships;
- co-operatives;
- Societas Europaea (SE, European Company);
- European Economic Interest Grouping (EEIG).

In addition, foreign persons may establish a branch in the Czech Republic.

A branch is not a legal entity, but must be registered in the Commercial Register.

The Act on Business Corporations regulates the status and activities of entrepreneurs and applies to both legal entities and individuals.

A Czech legal person is an entity that has its registered office in the Czech Republic.

Foreign persons are defined as persons (individuals or legal entities) domiciled abroad or having their registered office outside the Czech Republic.

A foreign person's authorisation to carry out business in the Czech Republic takes effect on the date it is recorded in the Commercial Register. This does not apply to citizens of the member states of the EU, the EEA or Switzerland, their family members who have Czech residence permits, citizens of other states with long-term residence in the EU and their family members with long-term residence permits.

A foreign person may participate in the establishment of a Czech legal entity or become a partner or member of an existing Czech legal entity. A foreign person may also be the sole founder of a Czech legal entity, provided that Czech law permits a company to have a sole founder or sole shareholder.

The main characteristics of the various legal entities are described below.

Limited liability company (*společnost s ručením omezeným – spol. s r. o. or s. r. o.*)

- The company must have at least CZK 1 of registered capital.
- The list of shareholders, the amount of each shareholder's contribution and the names of the members of the supervisory board (if one is established) must be recorded in the Commercial Register.
- The law allows the creation of different kinds of shares. Shares to which the same rights and obligations are attached form one kind of share. Shareholders may own more than one share and also different kinds of shares.
- The shares of a shareholder may be represented by a common share certificate (*kmenový list*). However, such a certificate cannot be in the form of a registered certificate and may not be publicly offered or admitted to trading on the regulated market.
- A supervisory board is only necessary if required by the memorandum of association.
- The general meeting appoints an executive (*jednatel*) or executives, who are legally responsible for the management of the

company and whose details, including information on their authorisation to act on behalf of the entity, must be recorded in the Commercial Register.

- A legal entity may also be appointed as the executive.
- A limited liability company does not require an audit unless two or more of the following criteria are met, for both the year in question and the preceding year:
 - net turnover exceeds CZK 80 million per annum;
 - total assets exceed CZK 40 million;
 - the average number of employees exceeds 50.
 - Establishment takes around 1 month from providing all necessary documents and information.



Joint-stock company (*akciová společnost – a. s.*)

- Registered capital may not be less than CZK 2 million or EUR 80,000.
- Non-cash contributions to registered capital must be valued by an independent expert proposed by the founders (when a company is being established) or the company (registered capital increase). The valuation is binding on the company.



- A joint-stock company requires an audit if one or more of the following criteria are met for both the year in question and the preceding year:
 - net turnover exceeds CZK 80 million per annum;
 - total assets exceed CZK 40 million;
 - the average number of employees exceeds 50.
- Annual financial statements must be published.
- The company may decide between two internal structures: either a supervisory board and a board of directors (dualistic organisation of corporate bodies), or an executive director and a managing board (monistic organisation of corporate bodies). The chairman of the managing board may be the same person as the executive director. A legal entity may also be appointed as member of a board of directors.
- The names and addresses or the registered offices of the partners must be registered in the Commercial Register.
- All partners are entitled to act on behalf of the partnership and are jointly and severally liable for the partnership's obligations to the extent of their entire property.
- Audit requirements are the same as for a limited liability company.

Limited partnership (komanditní společnost – kom. spol. or k. s.)

- A limited partnership is formed by two or more persons (individuals or legal entities). At least one of the partners must be a general partner, with unlimited liability for the debts of the partnership. At least one partner must be a limited partner, liable for the partnership's debts only up to the amount of unpaid contributions recorded in the Commercial Register.
- The names and addresses or registered offices of the partners, a statement on whether they are limited or unlimited partners, the amount contributed by each limited partner and the amount of their paid up contributions must be recorded in the Commercial Register.

General partnership (veřejná obchodní společnost – veř. obch. spol. or v. o. s.)

- A general partnership is formed by two or more persons (individuals or legal entities).
- The partners in a general partnership are liable for the debts of the company.

- Only unlimited partners are permitted to manage the partnership.
- Audit requirements are the same as for a limited liability company.

Co-operative (družstvo)

- Co-operatives are formed by at least three members, either legal entities or individuals, to undertake business activities for the economic or social benefit of their members.
- Members are not liable for the obligations of the co-operative; however, the co-operative may demand contributions from its members to cover losses.
- Audit requirements are the same as for a limited liability company.

Branch of a foreign person (organizační složka zahraniční osoby)

- Branches of foreign businesses can conduct business activities in the Czech Republic if they are registered in the Commercial Register.
- The entry in the Commercial Register must include details about the activities of the foreign business and its office in the Czech Republic, the scope of its

business activities and the name and the address of its director (general manager).

- A branch must obtain a trade licence from the regional Trade Licensing Office.
- The liability of a branch is not limited.
- Audit requirements are the same as for a limited liability company.

Company formation procedure

- memorandum of association;
- obtention of trade license;
- contribution payment;
- registration in Commercial Register.

A company is formed after a founder's deed or a memorandum of association has been completed and signed. Limited liability companies and joint-stock companies must provide these documents in the form of notarial deeds.

After the founder's deed or memorandum of association has been signed and filed, the future executives of the company must register their trade licences at the Trade Licensing Office and obtain the documents necessary to register the address of the company.

The company's founders also need to name a contributions administrator, who will be responsible for proving to the Commercial Register that the contributions to the registered capital have been paid up by the shareholders.



After the future executives have collected all necessary documents, they may file an application for registration of the company in the Commercial Register. Once the court administering the Commercial Register registers the company, the process of the company's formation is complete. The whole process may take up to two months.

The Commercial Register

A company has legal status and is entitled to commence business activity in the Czech Republic only after it has been registered in the Commercial Register. Courts have five business days to register the company in the Commercial Register after the application is submitted. Fees amount to CZK 6,000 for a limited liability company and CZK 12,000 for a joint-stock company (approx. EUR 220 and 440).

Entries in the Commercial Register include the name of the entity and the address of its registered office, the identification number of the entity, the scope of its business activities, the type of entity and the names and addresses of the executives or directors, together with details of their authorisation to act on behalf of the entity.

Access to the Commercial Register is freely available on the internet (www.justice.cz; www.info.mfcr.cz/ares).





***Cibulák /tsibulák/**
Cibulák china

Traditional porcelain decorated with an onion pattern. It is hand-decorated and its key motif is usually an aster or peony and the edges of the chinaware are decorated with compositions of peaches and pomegranates. The first Czech cibuláks were produced in 1885.

Employment policy

The Czech Republic has a skilled and educated labour force and its literacy rate is above 98 percent.

Czech labour law is not considered excessively rigid and is relatively flexible within the EU context.

Employment law is governed by the Labour Code. Where an employee from another EU member state is sent by an employer to work in the Czech Republic as part of the transnational provision of services, Czech Labour Code regulations shall apply to basic conditions, such as maximum working hours and the minimum length of rest periods, the minimum annual leave entitlement, the minimum wage and overtime rates, occupational health and safety, etc.

The maximum working week is 40 hours. The standard working week is Monday to Friday.

The maximum amount of overtime which may be ordered by the employer is 150 hours per year. The maximum amount of overtime worked with the employee's consent may not exceed 416 hours annually. Overtime must be distributed evenly.

The retirement age for individuals ranges from 60 to 65 based on gender, date of birth and the number of children raised (applicable to women only).



Employment contracts

Employers are required to conclude written employment contracts with their employees. The contract must at least describe the type of work, the date the employee will commence work, and where the work will be performed. Trial periods may generally not be longer than three months, except for managerial positions, where they may extend to up to six months. A fixed-term employment contract may be concluded for up to three years, and may only be renewed twice.

An employment contract concluded for an indefinite period or a fixed term may be terminated:

- by agreement;
- by notice;
- by immediate termination;
- by termination during the trial period.

A fixed-term employment contract also terminates on the expiry of the agreed period.

The employer or the employee may terminate a contract by giving written notice. The notice period for the employer and the employee is at least two months, and the employee can give notice without stating a reason.

When the employer terminates an employment contract, it must be for one of the reasons stated in the Labour Code, such as:



- The employer is being liquidated or is ceasing to carry on business.
- The employer is relocating.
- The employer is undergoing organisational changes.
- The employee has committed a serious disciplinary breach.

Where an employment contract is terminated for any of the reasons under points 1 to 3, the employer is obliged to pay the employee up to three months' severance pay depending on the duration of the employment relationship.

Specific termination conditions apply in respect of temporarily disabled employees, pregnant women and employees caring for minors. Specific termination conditions, severance pay rules and other conditions may also be included in a collective agreement, if in force.

During the trial period, the employment contract may be terminated by either side for any reason, or without any reason being given.

Employment agencies

An alternative to employment contracts is agency employment.

An employment agency provides its clients with human resources, without the clients having to conclude employment contracts with the employees. Even though this option is more ex-

pensive, it provides flexibility in the allocation of human resources.

Mass layoffs

If an employer terminates the employment relationships of a certain number of employees as defined in the Labour Code, for the specific reasons set out above under points 1 to 3, within a period of 30 calendar days, this is considered a mass layoff and special conditions, such as a notification obligation to the Labour Office and unions, apply.

Trade unions

Unions can be formed freely and neither the state nor any other subject can restrict their formation.

Trade unions engage in collective bargaining at a national level. A tripartite council including representatives from trade unions, employers and the government meets annually to discuss labour issues.

The role of trade unions in the Czech Republic is to formulate and assure the labour, economic and social interests of employees. The aim is to reach an agreement with the employer based on the collective bargaining.

Holidays

An employee is entitled to holiday pay if the employment contract lasts for at least 60 consecutive days during a calendar year. For employment relationships shorter than a year, employees accrue one-twelfth of the annual holiday for each calendar month of continuous employment with the same employer.

The minimum holiday period is four weeks per annum, unless increased by a collective bargaining agreement, employment contract or internal regulations. Holiday pay is calculated on the basis of the employee's average monthly salary.

Social security and health insurance

There are two major schemes to which both the employee and the employer must contribute: social security and health insurance.

Payments from the social security insurance system typically include:

- pensions;
- cash benefits such as sick leave, maternity benefits, social benefits, etc.

A social security treaty is concluded with certain countries and removes the burden of paying social security contributions to both countries.

Concurrence of a function as a member of a corporation's statutory body and employment

Current legislation does not allow the concurrence of the membership in a statutory body (executive officership) and employment.





***Jitrnice /jitrnitsə/
Liver sausage**

Also called jetrnica in Moravia. Made of pork meat and offal, it belongs among one of the most typical foods at a Czech pig slaughter, a traditional autumn feast at which domestic pigs are slaughtered and their meat is processed into various home-made food products stored for the winter.

Financial services

The Czech financial sector: a safe harbour for foreign investments (continuing profitability, sufficient liquidity, as well as capital adequacy).

Regulation and supervision

The Czech National Bank (CNB) is the central bank of the Czech Republic. It determines the country's monetary policy, carries out and coordinates the supervision of the Czech financial market, issues banknotes and coins, and manages the circulation of currency as well as the payment and settlement systems between banks. More details can be found at: www.cnb.cz.

The responsibility for preparing primary legislation for the financial market sector mainly lies with the Ministry of Finance; the CNB assists in this process.

As the Czech Republic is an EU member, in the area of supervision the CNB cooperates with European institutions (the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority) on unifying supervisory procedures and creating conditions for close cooperation between home and host supervisors. The CNB also closely cooperates with the European Central Bank in its role of banking supervisor within the Single Supervisory Mechanism.

Prudential rules for banks, credit unions and investment firms are primarily regulated by the Capital Requirements Regulation (CRR) directly

applicable in EU member states and a decree issued in 2014 driven by measures agreed on at the EU level and implementing the requirements of Basel III/CRD IV into Czech legislation. Solvency II, a new, harmonised EU-wide insurance regulatory regime, will be effective from 1 January 2016 in all EU member states, including the Czech Republic.

Licences

The licensing of banks and other financial institutions and matters connected with mergers and acquisitions and other market entries are fully within the responsibilities of the CNB.

A foreign financial institution can enter the Czech market in the following four ways:

- as a new company, with up to a 100 percent foreign ownership;
- by acquiring an equity stake in an existing entity;
- by establishing a branch of the parent institution with a separate licence;
- by establishing a financial institution of the parent based on the licence of the parent institution (applicable to all banks and insurance companies with a registered office in the EU under the "single licence principle").



Deposit insurance

Since 2010, the deposit limit for 100-percent protection has risen to EUR 100,000. The deposit claims of banks, foreign banks, financial institutions, health insurance companies and state funds are not insured.

All banks and branches of foreign banks (excluding branches of parent banks participating in the deposit insurance scheme in their parent country) are obliged to participate in the scheme and to contribute to the deposit insurance fund in compliance with the Act on Banking.

Banking sector

The Czech banking sector is primarily represented by banking institutions with international ownership. It is dominated by big foreign banking groups such as Erste, KBC, Societe Generale, UniCredit, Raiffeisen or GE Money. Although the banking sector is significantly concentrated, small and medium banks have been able to strengthen their position on the Czech market in previous years.

Typical activities include commercial lending to corporate and retail clients, customer accounts and deposits administration, credit card operations, international lending and loan syndications, mutual funds management and administration, bank treasury operations and back office activities.

As at 30 September 2015, 47 banks (including foreign branches) offered banking services to clients in the Czech Republic; 39 of them were controlled by foreign investors and eight by local stakeholders. The group of the four largest banks (banks with total assets greater than CZK 200 billion) played a predominant role in the banking sector in the Czech Republic. As at 30 June 2015, their share of total banking assets equalled approximately 58 percent.

Despite a low interest rate environment, the Czech banking sector maintained very good profitability in 2015. Net profits for the first half of 2015 exceeded CZK 37 billion (for the whole year of 2014 it was more than CZK 61 billion) with the level of non-performing loans at approximately 6 percent.

Profitability of the Czech banking sector

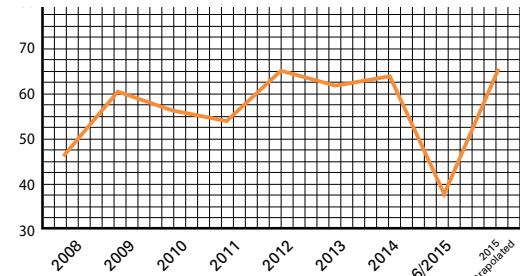


Figure 10: Net profit of the Czech banking sector, in billions of CZK
Source: http://www.cnb.cz/en/supervision_financial_market/aggregate_information_financial_sector/basic_indicators_financial_market/index.html



Insurance sector

The Czech insurance sector is dominated by the Generali and VIG insurance groups. The remainder of the TOP 10 insurance companies is made up by composite insurance companies, while the rest is represented by bank-assurance and specialised insurance companies.

As at 30 September 2015, 54 insurers (including foreign branches) and one reinsurance company offered insurance services to clients in the Czech Republic. Local shareholders controlled 14 insurance companies, whereas the rest had mostly foreign owners. The two largest groups reached CZK 74.2 billion of gross written premium (measured by annual premium equivalent). Overall market profitability is approximately a 12% return on equity (three-year average/2012 - 2015) and the market manages approximately CZK 480 billion of assets.

Typical products include both life and non-life insurance. The non-life insurance business is dominated by car insurance (compulsory motor third party liability insurance and casualty and collision (automobile insurance)) and commercial insurance.

The supervision of the insurance market is performed by the CNB.



Investment management and funds

As at 30 September 2015, the Czech market is represented by more than 350 investment funds domiciled in the Czech Republic, according to CNB statistics. In addition, approximately 1,300 foreign investment funds are registered for public offer in the Czech Republic.

According to an act adopted in 2013, extending options for establishing new investment funds in line with European regulations, investment funds may take the following legal forms:

- mutual fund;
- trust fund;
- joint-stock company;
- investment company with variable capital (société d'investissement à capital variable);
- limited partnership;
- limited liability company;
- European company.

Generally, minimum fund capital of EUR 1.25 million is required. The foundation of funds fulfilling EU requirements must be approved by the CNB. A notification duty to the CNB only applies to special investment funds not fulfilling these requirements. However, every fund's asset manager must have the approval of CNB.

The supervision of the investment fund market is handled by the CNB.

The stock exchange

The Prague Stock Exchange (PSE) began trading in April 1993. Trading on the PSE is conducted via licensed securities dealers, who are also PSE members.

These are primarily major banks and brokers. If a common investor decides to invest in the exchange, they need to contact one of the PSE members or become a member themselves.

It is currently possible to conclude trades either directly through the regulated market (administered by the PSE) or the non-regulated market, primarily intended for OTC (over-the-counter) trades (administered by the Central Depository). Since 2012, trades on the regulated market are traded via the stock international exchange platform – Xetra. The basic criteria for trading and listing on either market can be found at: www.pse.cz.

Foreign exchange

Regulation

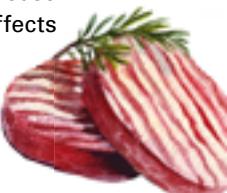
The Act on Foreign Exchange fully implemented the obligations which the Czech Republic accepted under international agreements in relation to the free movement of capital and the

system of payments. The Czech Republic has concluded many agreements with other countries on the promotion and reciprocal protection of investments.

Market development

The exchange rate of the Czech crown (CZK) to the euro (EUR) as well as to other main currencies was affected by the intervention of the CNB, which started in November 2013 (see Figure 11). The CNB announced its intention to keep the Czech currency below the level of 27 CZK/EUR. The intervention was primarily driven by the fact that inflation had been well below the inflation target for a prolonged period, potentially threatening deflation. The CNB subsequently announced that it will not discontinue using foreign exchange market intervention as a monetary policy instrument sooner than in the second half of 2016.

As is shown in the graph below, during 1H 2015, the CZK stayed around the threshold of 27 CZK/EUR set up by the CNB and the Czech crown significantly depreciated to 25.5 CZK/EUR against the US dollar (March/April 2015). These movements were caused by a weak euro due to the Greek crisis and the expected increase of interest rates by the FED. These two effects



resulted in the significant depreciation of EUR/USD.

As at 30 September 2015, the foreign exchange rate of CZK to EUR was 27.180; the exchange rate of CZK to USD was 24.266.

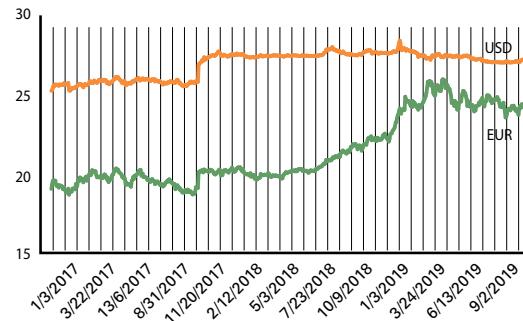


Figure 11: CZK development during 2013, 2014 and 2015 (CZK/EUR and CZK/USD)

Source: ČNB

Repatriation of capital and profit

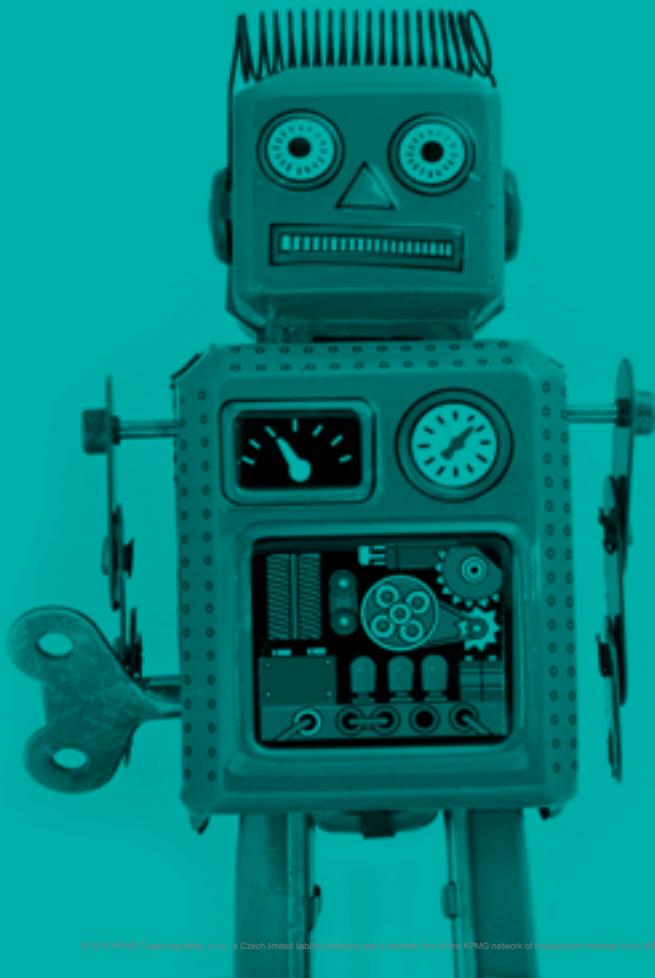
The Czech currency is convertible outside the Czech Republic. Czech companies may freely repatriate both current year profits and retained earnings in whatever currency they desire. However, they should follow the minimum capital requirements – if applicable – imposed by the CNB.

Branches of foreign banks do not have such limitations as the capital is managed and monitored centrally.

The following types of payments from a Czech company to its foreign parent may be transferred abroad freely, subject to the appropriate withholding taxes:

- dividends;
- interest;
- charges for intangible property (e.g. royalties and know-how fees);
- management fees;
- liquidation balances.





*Robot /rəbɒt/

A word denoting artificial beings akin to people, used for the first time by Czech writer Karel Čapek during the premiere of his play R.U.R. nearly 100 years ago. Čapek used the word robot following advice from his brother Josef.

Direct Taxes

The Czech Republic is party to a large number of double taxation treaties and has implemented the relevant EU directives.

Taxation of legal entities

Corporate income tax is levied on the profits of legal entities, primarily limited liability companies (*s. r. o.*) and joint-stock companies (*a. s.*). Although partnerships are also legal entities, the profits of a general partnership (*v. o. s.*) are not subject to corporate tax; instead, the partners' share of profits is taxed in their own hands.

In the case of a limited partnership (*k. s.*), the limited partner's share of the profits is subject to corporate income tax at the level of the limited partnership, while the general partner's share is taxed in the same way as in the case of a general partnership. In addition, trusts are subject to corporate tax even though they are not legal entities.

A branch or permanent establishment of a foreign company is generally subject to tax on the same basis as a company. They may also be taxed on a deemed profit basis, which is usually a percentage of the revenues generated in the Czech Republic, or a percentage of costs. Since most of these legal entities by definition exist for the purpose of carrying on a business, virtually all the income and gains they realise are included in the calculation of their business profits (see below). There are special rules for entities not established for the purpose of mak-

ing profits as these enjoy certain restricted tax privileges.

In 2016, the corporate income tax rate is 19 percent. A reduced rate of five percent applies to the income of qualifying investment funds and a reduced rate of 0 percent applies to qualifying pension funds. Full or partial tax relief from corporate tax may be claimed for certain qualifying investments (see *Chapter 3 – Investment incentives and state aid*).

Capital gains are generally included in income and taxed at the same rate. However, if at least 10 percent of the shares of a company are held by a parent company for 12 months, income from the sale of the shares is tax exempt if the parent is a Czech tax resident company and the subsidiary is resident in an

EU member state or a non-EU member state with which the Czech Republic has concluded a double taxation treaty (subject to certain conditions). Income derived by non-residents from the sale of shares in a Czech company is taxable, unless the seller is a company resident in the EU, Norway, Iceland or Liechtenstein, and at least 10 percent of the shares have been held for 12 months.

There is no tax consolidation in the Czech Republic. Each company within a group is taxed individually, with no set-off of losses against

the profits of a different company. However, virtual tax consolidation can be achieved through a partnership structure.

Dividends received by Czech resident companies from non-residents are taxed at a rate of 15 percent. They are exempt from tax if the payer is a company resident in an EU member state, provided that at least 10 percent of the shares have been held for 12 months.

The exemption also applies if all the following criteria are met:

- the payer is a tax resident of a state with which the Czech Republic has concluded a double taxation treaty;
- the payer has a similar legal form to a limited liability company (*s. r. o.*), joint-stock company (*a. s.*) or co-operative (*družstvo*);
- the recipient has held at least 10 percent of the shares for 12 months;
- the payer is subject to a tax similar to Czech corporate tax, and the rate is at least 12 percent.

Exemptions for capital gains and dividends do not apply if the parent company or the subsidiary are either:

- exempt from corporate income tax (or similar tax);

- able to claim a corporate income tax exemption or corporate income tax relief;
- subject to corporate income tax at a rate of 0 percent, or if the recipient is not the beneficial owner of the income.

An amendment regarding hybrid loan arrangements (i.e. payments which are treated as deductible expenses in the source state and as tax exempt dividends in the recipient state) is expected to be adopted during 2016, denying tax exemptions for such payments at the level of the recipient company.

Mergers and divisions of companies can generally be carried out on a tax neutral basis. The EU Mergers Directive and the EU Cross-Border Merger Directive have been broadly assimilated into Czech law. In general, domestic legislation maintains the tax neutrality of mergers and allows the transfer of unused tax losses for transactions satisfying certain legal conditions (transfers of business and mergers), provided that tax avoidance is not the main purpose of the transaction. Additionally, there is a "same activity" rule, under which tax losses can only be offset against income earned from the same economic activity that generated the tax loss.

Taxation of business income

The starting point for computing taxable profit is the profit before tax in the Czech statutory financial statements. This is then subject to adjustments under the Income Taxes Act. Unless this Act contains a provision to the contrary, income and expenses booked for accounting purposes are taxable/deductible. Where capital gains form part of business profits they are taxable as normal income or exempt under the participation exemption rules.

For companies, the tax year is generally the same as the financial year. It is possible to adopt a financial year ending on a date other than 31 December provided that it is the last day of a calendar month. If the financial year-end changes, provisions in the Income Taxes Act deal with the resultant long or short period. However, these are not perfectly drafted and numerous issues can arise in such cases. Individuals are always taxed on a calendar year basis.

The Income Taxes Act attempts to define which deductible and non-deductible expenses in some detail. The general rule is that expenses incurred for the purpose of generating, assuring or maintaining taxable income are tax deductible.

A special deduction equal to deductible expenditures on research and development (R & D) can be claimed and effectively means that such expenditure is deducted twice; this deduction, if not used in the period in which it arises, may be carried forward to the next three tax periods. The Act on Reserves allows restricted deductions for bad debt reserves. It also allows taxpayers to create tax deductible reserves for future repairs, subject to the existence of supporting evidence in the form of project plans, as long as the funds are transferred to a separate bank account by the due date for filing the annual tax return.

The Act on Reserves contains special rules on loan provisions for banks and reserves for insurance companies.

Tax depreciation can be claimed on fixed assets. For this purpose, fixed assets are divided into several categories broadly reflecting their expected useful life. Depreciation on most assets may be claimed on either a straight-line or an accelerated basis.

Tax losses may be carried forward for five years. Losses may not be carried forward following a substantial change in the direct ownership of a company unless it can be shown that at least 80 percent of the company's revenues are derived from the same activities as those carried

out in the period when the loss arose. A change of at least 25 percent in the ownership of registered capital or the voting rights, or a change resulting in a person obtaining a controlling influence in the company, is always considered a substantial change. Restrictions also apply in the case of certain corporate restructuring. A ruling may be obtained from the tax authority to confirm whether a loss may be utilized after a substantial change or restructuring.

Transfer pricing

As has been the case in other OECD countries, the review of transfer pricing policies has become one of the biggest priorities of the Czech tax authorities. The focus is not only driven by global BEPS (Base Erosion and Profit Shifting) initiatives, but also by the general focus of the state administration on increasing the compliance of companies with valid regulations and arm's length principles.

Czech legislation is relatively simple in this area. Transfer pricing is dealt with in a short provision that states that if prices agreed in transactions between related parties are not at arm's length and the difference is not properly justified, the tax base should be adjusted. It is possible to request unilateral or bilateral advance pricing agreements from the tax au-

thorities regarding the method of setting the transfer price between related parties. No retroactive agreements are possible.

In addition to the provisions of the Income Taxes Act, the Ministry of Finance has issued guidelines providing more detailed information especially on transfer pricing documentation (e.g. Decrees D-332, D-333, D-334 and D-10). These are not legally binding, but given that the tax authorities usually follow them, they represent useful guidance for taxpayers.

Companies are also required to disclose various types of related party transactions, including the volumes realized with each related party, in an appendix to the corporate income tax return.

This disclosure obligation falls upon Czech tax payers who meet one of the three criteria listed below:

- assets totalling more than CZK 40 million;
- a net turnover of more than CZK 80 million;
- a recalculated headcount exceeding 50 employees.

The obligation is further limited to companies meeting the above criteria, which either:

- performed transactions with related parties abroad;
- incurred tax losses;
- are recipients of investment incentives.

There is currently no legal obligation to have transfer pricing documentation prepared. However, the tax authorities regularly require transfer pricing documentation to be provided during tax inspections with the usual deadline of 15-30 days.

Thin capitalisation

Thin capitalisation provisions act to restrict the deductibility of interest and other loan expenses where the borrower has insufficient equity. The rules can be summarised as follows.

- Financial expenses (including interest) arising from loans and credits received from related parties in excess of four times (six times for banks and insurance companies) the borrower's equity are not tax deductible.
- Interest on loans and credits received from unrelated parties, or those secured by a related party, is fully deductible on general principle, except for interest on "back-to-back" loans (i.e. where a related party provides a loan, credit or deposit to an unrelated party which then provides the funds to the borrower), which is treated as interest on related party debt.
- Where interest or other revenue is derived from the borrower's profit,

all financial expenses on the loans or credits received are non-deductible.

Any upward adjustment of profit resulting from a transfer pricing or thin capitalisation adjustment relating to a non-EU or EEA resident counterparty may be treated as a dividend, i.e. is subject to dividend withholding tax, as reduced by the provisions of any applicable double taxation treaty.

Taxation of individuals

Individuals are subject to income tax, social security, health insurance, and taxes on land and buildings. The taxation of individuals primarily depends on their residence status. Residents of the Czech Republic are subject to tax on worldwide income, whereas non-residents are subject to tax on Czech source income only.

Czech tax residence is defined as either:

- having a permanent home in the Czech Republic;
- spending 183 days or more in the Czech Republic during the tax year (the year to 31 December).

Personal income tax is charged on:

- employment income;
- business income;
- investment income;
- rental income;

- capital gains;
- any other income not in the above categories.

There are numerous exemptions, the most important of which are the exemptions from tax on gains from the sale of shares and securities.

- Gains on the sale of securities acquired before 31 December 2013 are exempt if the securities have been held for more than six months and do not represent more than five percent of registered capital and voting rights for 24 months preceding the sale.
- Gains on the sale of securities acquired before 31 December 2013 representing more than five percent of registered capital and voting rights and any securities acquired on or after 1 January 2014 are exempt if they were held for three years.
- Generally, no tax is payable if the income from the sale of securities does not exceed CZK 100,000 in a tax year.
- Gains on the sale of shares in a limited liability company are exempt if the shares were held for five years.
- Gains from the sale of non-business real estate are exempt if the property was held by the taxpayer for at least five years prior to the sale. Gains from the

sale of a dwelling are also exempt if the dwelling was used as the taxpayer's main residence for at least two years. If it was used for less than two years, the exemption applies if the gains are to be used for the taxpayer's housing in the future.

From 2015, exempt income exceeding CZK 5 million in a given tax year must be declared to the tax authorities.

The income of individuals is subject to a flat tax rate of 15 percent. An additional seven percent (a "solidarity tax increase") is applied on income (either the gross salary or the self-employment tax base) in excess of the maximum annual assessment base for social security contributions (CZK 1,296,288 in 2016). The 15% percent flat tax on employment income is calculated on the basis of the super-gross salary, which is the gross salary increased by social security and health insurance contributions payable by the employer. Employment income of individuals who are not subject to Czech social security that is taxable in the Czech Republic is increased by the amount of an employer's deemed contributions regardless of the amount of social security and health insurance contributions actually paid. Thus, the effective tax rate is not 15 percent (or 22 percent for per-

sons subject to the solidarity tax) but a higher rate, depending on the income level.

Dividends and certain types of other Czech source income are taxed separately and are subject to a 15 percent withholding tax at their source.

Foreign source investment income should be included in the tax base and is subject to a flat tax rate of 15 percent.

Business income or other self-employed income may be reduced by actual expenses or by an optional lump-sum deduction ranging from 30 to 80 percent of gross income. The annual lump-sum deduction is limited to a maximum of CZK 1,600,000 for income from agricultural business, CZK 1,200,000 for business income based on a trade license, CZK 600,000 for rental income and CZK 800,000 for other business income.

Employees are subject to tax on income in all forms, whether in cash or in kind. In particular, benefits, such as the provision of a car available for both business and private use, are taxable. It is not possible to deduct an employee's social security and health insurance contributions from the tax base. However, items such as mortgage interest, payments for supplementary pension insurance with state support, private life insurance premiums, and donations can be deducted if certain conditions are met.

Employer contributions to defined private pension schemes up to CZK 30,000 per year are tax free for the employee.

The Czech pension system comprises two pillars – a mandatory pay-as-you-go pension system run by the government (the first pillar) and a voluntary additional pension system administered by commercial insurance companies (the third pillar). A second pillar which involved optional payments of part of the mandatory obligations to private pension funds, was abolished with effect from 1 January 2016.

There are no special provisions dealing with employee share option schemes and gains realised on exercising an option are regarded as taxable income. It is generally accepted, however, that no gain arises on the granting of an option.

The salaries of employees are usually subject to the deduction of wage tax withheld by their employer on a monthly basis, with possible annual reconciliations. It is possible to second expatriate staff through a permanent establishment of a foreign employer that, although taxable, is not registered in the Commercial Register. In such cases, no liability to withhold tax arises. Instead, the employees themselves are liable to file tax returns and pay tax, normally in quarterly instalments.

Employees of foreign companies may fall under a further possible tax treatment, the “deemed employer” rule, which is essentially an anti-avoidance provision.

The rule may apply if employees of a foreign employer work in the Czech Republic under the control of a Czech person who pays a fee to the foreign employer for their services. Here, the Czech person is regarded as the employer for tax purposes and has to account for the employees’ income tax.

In practice, this rule is rarely applied to employees of bona fide foreign investors, unless they choose to use it as an alternative to the permanent establishment described above. Further special treatment applies to licensed labour agencies.

Resident and non-resident individuals may claim a basic personal tax allowance of CZK 24,840 per year. Various other credits are granted to a resident, such as a tax credit of CZK 24,840 per year for a spouse living in the taxpayer’s household if the spouse’s annual income does not exceed CZK 68,000 and tax allowances for children (a tax allowance of CZK 13,404 for the first-born, CZK 15,804 for the second-born and CZK 17,004 for the third-born

and any subsequent child¹). Tax allowances up to the amount of the minimal wage announced for a given tax year (CZK 9,900 for 2016) can be claimed for fees paid to child care facilities.

Limitations apply to individuals earning business or rental income, who claim flat rate expense deductions.

Allowances are also granted to residents of the EU or EEA if at least 90 percent of their income is derived from sources in the Czech Republic. The amount of income from foreign sources should be confirmed by the foreign tax authorities in the state of residence.

Social security contributions, where payable, amount to 45 percent of an employee’s salary (for income up to an annual cap for social security – see below). This consists of an employee contribution of 11 percent and an employer contribution of 34 percent, made up as follows.

	Employer (%)	Employee (%)
Pension	21.5	6.5
Sickness insurance	2.3	0.0
Unemployment insurance	1.2	0.0
Health insurance	9.0	4.5
Total	34.0	11.0

¹ According to a proposed amendment to the Income Taxes Act which is expected to be passed during 2016, the allowance for the second-born child will increase to CZK 17,004 and that for the third and any subsequent child will increase to CZK 20,604. The increased allowances should apply for the whole of 2016.

The maximum annual assessment base for social security premiums in 2016 is CZK 1,296,288. There is no cap on health insurance premiums. Social security and health insurance contributions must be paid on a monthly basis. Social security contributions must be paid until the aggregate of the monthly assessment base exceeds the maximum annual assessment base. Upon achieving this limit, the employer should stop paying social security contributions. The assessment base is very similar to the tax base. Foreign persons under local employment contracts are subject to Czech social security. Foreign persons employed by a non-Czech employer, with a social security treaty between the Czech Republic and the country of the employer in place, are subject to Czech social security unless, under the terms of the treaty, they can remain in the social security system of the home state.

The authorities take the view that expatriate employees of EU employers are subject to Czech social security based on EU social security rules. In practice, this means that expatriates are liable to Czech contributions unless they remain in their home state system under EU rules.

Tax on the acquisition of immovable property

Tax liability arises upon the registry of the transfer of the ownership in the land register. The tax is payable by the transferor (seller), although the parties can agree that it will be paid by the acquirer².

The tax rate is four percent of the tax base. The tax base is the higher of the agreed price (including VAT if applicable) and of a reference value. The reference value is calculated by tax authorities based on prices for similar transactions. If the tax authorities cannot calculate a reference value, the tax base will be the higher of the agreed price and 75 percent of the value assessed by an expert. If real estate is transferred as part of an enterprise, the tax base will be based on an expert valuation.

The taxpayer must submit a tax return by the end of the third month following the month in which the transfer was registered. The tax is due by the same deadline. Tax declared in the return is in some cases considered a pre-payment and is subject to review by the tax authorities.

² According to a proposed amendment, which should become effective as of 1 April 2016, the acquirer of the real estate should always be the tax payer.

Taxation of income from inheritance and gifts

From 1 January 2014, gift and inheritance taxes have been abolished and the taxation of such income is now governed by the Income Taxes Act. Gifts are taxable unless the donor is a qualifying spouse or close relation and are subject to a flat rate of 15 percent for individuals and 19 percent for companies. No tax is payable on inherited property.

Tax on immovable property

Tax on immovable property is payable by owners of immovable property situated in the Czech Republic. This tax is generally small compared with other developed countries. Different rates apply to land and buildings.

The property tax on buildings used for business purposes is based on the area of the buildings, using the rates below.

	CZK/m ²
Residential and agricultural	2
Industrial	10
Other business	10

An additional charge of CZK 0.75 per square metre is levied for each storey (above the

ground floor) of a building used for business purposes if the area of the storey exceeds one third of the area of the ground floor.

Real estate tax on agricultural land is 0.75 percent of the deemed value. Special rates apply for forests, lakes and ponds. For other types of land, the tax is based on the area, and the rate is CZK 2 per square metre for building plots, CZK 5 per square metre for improved land surface used for business purposes and CZK 0.20 per square metre in other cases.

For some types of property, the rates are multiplied by a coefficient ranging from 1 to 5 depending on the location of the property. In addition, the tax can be increased by another coefficient, varying from 2 to 5, based on the decision of the relevant municipality.

International tax issues

A company's registered office is the place where the effective management of the company is located. Companies with their registered office in the Czech Republic are subject to Czech tax on their worldwide income and are referred to as Czech residents.

Other companies (non-residents) are subject to tax only on their Czech source income, subject to the provisions of any double taxation treaties.

Foreign source income of Czech resident companies is generally taxable in the Czech Republic, subject to the provisions of any double taxation treaties. The income of foreign branches or permanent establishments of Czech residents is included in their taxable profit. Dividends from foreign companies are a separate source of income taxable at a special rate of currently 15 percent, unless the Parent-Subsidiary Directive applies.

Under certain double taxation treaties, however, the foreign income of Czech residents is exempt from Czech tax. In such cases, expenses related to that income are not tax deductible. Credit for foreign taxes on income that is also subject to Czech tax is available only if a double taxation treaty exists with the other state. Otherwise, the foreign tax can only be treated as an expense.

The main types of Czech source income for non-residents are:

- income of a permanent establishment in the Czech Republic;
- income from a dependent activity (employment) performed in the Czech Republic;
- income from services provided in the Czech Republic;

- income from the sale or use of real estate situated in the Czech Republic;
- royalties, dividends and other profit distributions, interest, and lease rentals;
- income from the transfer of shares in Czech resident companies not tax exempt under domestic legislation;
- income from the sale of a business as a going concern located in the Czech Republic.

These tax liabilities are to some extent mitigated by tax treaties, where applicable. In particular, if there is a treaty in place, then:

- Income from services can usually be taxed only if the service provider has a permanent establishment in the Czech Republic.
- Income from employment can usually be taxed only if the employee is employed by a Czech company or a Czech permanent establishment of a foreign company, or if they spend more than 183 days in the Czech Republic.

Income liable to tax is generally subject to withholding taxes at a rate of 15 percent. The rate is increased to 35 percent if the income is paid to residents of countries which have not signed a double taxation treaty with the Czech Repub-

lic, when no arrangement is in place for the exchange of information on tax matters.

Withholding tax is a final tax that is generally reduced by double taxation treaties. Residents of other EU and EEA countries can file a tax return in respect of some types of income (e.g. interest, royalties, freelance work) subject to withholding tax and claim a deduction for any related expenses (this does not apply for withholding tax from dividends). In such a case, the withholding tax is considered an advance payment. This may result in a reduction in the tax burden as withholding tax is calculated on a gross basis.

The EU Parent-Subsidiary Directive has been implemented in the Czech Republic, which means that dividends paid by a Czech subsidiary to a parent company that is a tax resident in an EU member state may be exempt from withholding tax. These provisions also apply to dividends paid between Czech companies and dividends paid to Swiss, Norwegian, Icelandic and Liechtenstein corporate shareholders.

The EU Interest and Royalties Directive has also been implemented in the Czech Republic. As a result, interest and royalties paid to some associated companies resident in the EU, Switzerland, Norway, Iceland and Liechtenstein are

generally exempt from withholding tax (subject to advance clearance procedures).

The Czech Republic has implemented the EU Savings Directive, which allows the provision of information about interest paid by Czech financial institutions to non-residents.

Other types of income paid to non-EU or EEA residents, notably from permanent establishments, real estate and sales of securities, etc., are subject to withholding tax which is not the final tax, but a prepayment in respect of the ultimate tax liability. This tax is generally levied at the rate of 10 percent (one percent for sales of securities or payments for receivables purchased from third parties), but may be reduced by prior negotiation with the tax authorities.

Beneficial ownership concept

A number of double taxation treaties concluded by the Czech Republic expressly limit their benefits to the beneficial owners of income.

In situations where an investor in the Czech Republic is a foreign entity or a trust that is tax transparent under its own tax laws, the Czech Republic will generally honour its transparency for the application of the Income Taxes Act and double taxation treaties. The income paid from Czech investments will normally be treated as

the income of the ultimate beneficial owner of the investment via the transparent entity.

Tax administration

The administration of tax is mainly governed by the Tax Code with specific procedures provided by other Acts.

All Czech resident companies, limited partnerships, and permanent establishments of non-resident companies must file tax returns. This does not apply to general partnerships, where the partners declare their share of partnership profits.

All individuals with an annual taxable income exceeding CZK 15,000 must file tax returns unless the income is tax exempt or subject to withholding tax. A return must also be filed by any individual who is liable to the solidarity tax. This means that, in general, low-paid employees of Czech companies or branches of foreign entities are not required to file returns unless they have other taxable income.

Anyone who claims a tax loss must also file a return.

The deadline for the submission of a tax return is three months from the end of the taxable period. For all taxpayers, with the exception of legal entities that have adopted a non-calendar year-end, the taxable period is the calendar

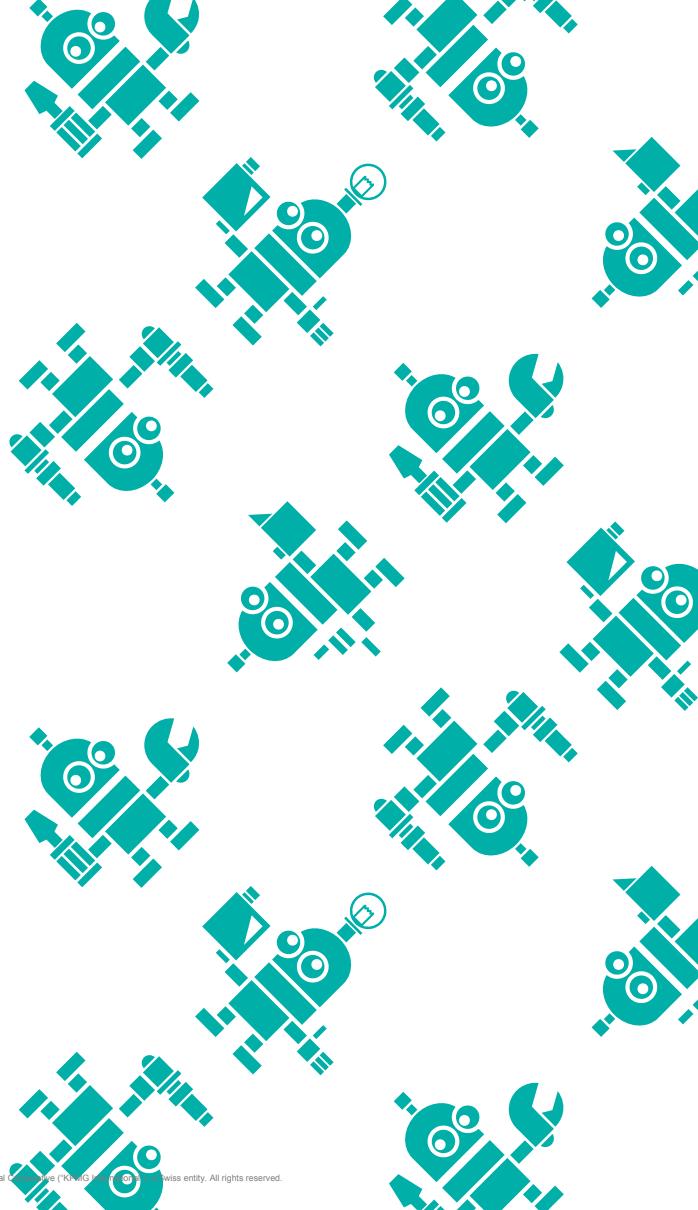
year, and the tax return deadline is therefore 1 April. **This deadline is extended by a further three months if:**

- the taxpayer is subject to a statutory audit;
- the taxpayer engages a registered tax advisor to submit the tax return on its behalf.

Except for withholding tax, income tax is collected during the year by a system of prepayments based on the previous year's liability. The final deadline for settling the liability is the same as for the submission of the return. The tax is treated as paid when it is received by the tax authority.

The tax authority has the power to carry out tax inspections to establish or examine the tax base or any other circumstances decisive for the correct determination of the tax liability.

Tax may not be assessed or additionally assessed after three years have elapsed from the deadline for filing the ordinary tax return. However, the deadline for the assessment of additional tax may be extended to a maximum of 10 years under certain circumstances, such as the filing of an additional tax return or the occurrence of a tax audit. In the event of some tax-related crimes, additional tax may be assessed regardless of the lapse of the period for tax assessment.



For taxpayer declaring a loss, the period in which a tax audit may be carried out is extended by the period during which the loss may be utilised. Since losses may be carried forward for up to five years, if extended deadlines apply, an audit can be carried out up to 15 years after the tax return became due.

If an appeal is lodged against an assessment, the payment of any additional tax is deferred until the payment order becomes legally effective, but interest continues to be calculated on the outstanding amount.

Interest on overdue tax is assessed at the Czech National Bank repo rate plus 14 percent, starting on the fifth working day following the due date. Where additional tax is assessed, a penalty of 20 percent of the additional tax is levied. If the tax authorities reduce a VAT refund, they will levy a penalty of 20 percent of the reduction. If a tax loss is reduced, one percent of the reduction becomes payable as a penalty. If the taxpayer corrects the tax base in an additional tax return, only interest on the overdue tax is payable.



***Kostkový cukr**
/kostkɔv̄i: tsukr/ Sugar cubes

Sugar processed into small cubes. As late as until the mid-19th century, sugar was commonly distributed in the form of sugar loaves. Sugar cubes are said to have been invented by Jakub Kryštof Rad, director of a sugar company in the town of Dačice. He was awarded a patent in 1843.

Indirect Taxes

The Czech VAT system is based on the harmonised principles of EU Directive 2006/112.

Value added tax (VAT)

The Czech Value Added Tax Act is based on the general principles of EC Directive 2006/112 and as such is very similar to other EU countries.

VAT is generally due on supplies of goods or services, intra-community acquisitions of goods and imports of goods with the place of supply in the Czech Republic.

VAT rates

The standard VAT rate is 21 percent (effective from 1 January 2013). The Czech Republic also applies two reduced rates. The first reduced rate of 15 percent applies to e.g. food products, public transportation services, social housing construction, and transfers of social housing, unless these are tax-exempt. The second reduced rate of 10 percent (effective since 1 January 2015) applies to essential baby nutrition, pharmaceuticals for human and veterinary purposes, books, mill products and their mixtures for the production of foods for gluten-intolerant individuals.

Exports and intra-community supplies of goods, as well as the international transport of goods relating to exports or imports of goods, are zero-rated.

Certain supplies of goods and services are exempt from VAT, for example:

- insurance and financial services;
- postal services;
- education;
- health and welfare services;
- transfer and financial leasing of immovable property under certain conditions;
- renting of immovable property (apart from short-term leases, leases of parking spaces and leases of safe deposit boxes).

VAT registration

VAT registration is obligatory for taxable persons established in the Czech Republic whose turnover for the preceding 12 consecutive months exceeded CZK 1 million. Other situations may also lead to obligatory VAT registration (e.g. the purchase of a going concern from a VAT payer, the transfer of the assets of a dissolved or spun-off VAT payer entity to a taxable person).

A taxable person not established in the Czech Republic becomes a Czech VAT payer if they make a specific transaction with the place of supply in the Czech Republic, such as a zero-rated supply of goods to another EU member state or a Czech local taxable supply (supply of goods, provision of services) on which they

have to account for VAT (i.e. the reverse-charge regime is not applicable). No registration threshold applies.

Taxable persons (both established and not established in the Czech Republic) may voluntarily register for VAT.

A group of related parties established or having a VAT establishment in the Czech Republic may register as a single VAT payer (group registration).

Persons identified for VAT

A taxable person who is not a VAT payer can become a person identified for VAT if they purchase a specific type of supply, where the place of supply is in the Czech Republic, e.g. they acquire goods from another EU member state, or they supply services where the place of supply is determined in another EU member state under the general rule. The person identified for VAT is obliged to account for VAT on the received supply; however, they are not entitled to claim related input VAT.

Reporting requirements

VAT returns

In general, VAT returns have to be submitted electronically on a monthly basis. Under certain circumstances, VAT payers can opt for

a quarterly period. However, a quarterly period is not possible for VAT groups and taxable persons whose turnover exceeds CZK 10,000,000 in the previous calendar year.

VAT returns must be submitted by the 25th day of the month following the relevant tax period. VAT payers who are not established in the Czech Republic and do not have a VAT establishment in the Czech Republic and persons identified for VAT are only required to submit VAT returns for VAT periods in which they performed taxable or zero-rated transactions.

VAT must be paid by the due date for submitting the VAT return. If there is excess input VAT, VAT credit should be paid to the VAT payer within 30 days of the deadline for submitting the VAT return.

The VAT returns must be submitted electronically via special-purpose application.

There is a penalty for non-submission/delay in submission of a VAT return (max. CZK 300,000) and penalty interest applies for late payment of VAT (14.05 percent p.a.).

EC Sales Lists

An EC Sales List must be completed if a VAT payer or person identified for VAT (where applicable) either:

- supplies goods from the Czech Republic to another EU member state to a person registered for VAT in another EU member state;
- moves their own goods from the Czech Republic to another EU member state;
- acts as the intermediary in a triangular transaction between VAT registered traders in other EU member states;
- provides a service to a customer established in another EU member state, where the place of taxable supply is determined in that EU member state under the general rule.

The EC Sales List should be submitted electronically on a monthly basis, within 25 days of the end of the month in which the supply takes place. Quarterly VAT payers, who only provide services as described in point 4 above, may submit EC Sales Lists on a quarterly basis.

VAT Ledger Statement

Since 1 January 2016, Czech VAT payers are obliged to file a VAT Ledger Statement which is considered an effective tool to detect and prevent tax evasion and fraud. The VAT ledger statement is filed electronically on a monthly or quarterly basis (depending on the status of the VAT payer) within 25 days after the end of

a VAT period. **VAT payers are obliged to report particular data about:**

- local supplies;
- local purchases;
- acquisition of goods from another EU member state and supplies acquired from persons not established in the Czech Republic;
- supplies (both received and provided) under the local reverse charge regime.

The VAT Ledger Statement does not substitute VAT return or the EC Sales List.

Intrastat declarations

Businesses dispatching goods to or receiving goods from other EU member states and exceeding relevant annual thresholds (CZK 8 million for dispatches or CZK 8 million for goods received) must complete and file an Intrastat declaration.

Intrastat declarations are submitted on a monthly basis, by the 12th working day of the month following the month for which the declaration is being filed. Intrastat declarations must be submitted electronically. A penalty of up to CZK 1 million may be imposed for failing to submit an Intrastat declaration.

Recovery of input VAT

In general, a Czech VAT payer is entitled to deduct input VAT in respect of received supplies used for the VAT payer's own business activity. Input VAT can be claimed within three years after the end of the tax period in which the taxable supply was made. A VAT payer must have a VAT invoice to exercise the right to deduct input VAT (a VAT document).

A VAT payer is generally not entitled to deduct input VAT on taxable supplies used for VAT exempt supplies, representation (entertainment) or non-business purposes.

A partial VAT deduction could be claimed in respect of taxable inputs related to both types of supplies, i.e. those qualifying for deduction of input VAT and those not qualifying for deduction (e.g. exempt supplies or non-business use).

The Czech Republic has implemented the general provisions of EU directives in respect of VAT refunds for entities registered for VAT purposes in other EU member states or non-EU businesses. VAT incurred in the Czech Republic is recoverable under the same conditions that apply to Czech VAT payers.

The application for a VAT refund should be filed electronically in the state where the taxable person has a registered office or place of busi-

ness. The application must be submitted by 30 September of the year following the year in which the VAT was incurred.

Non-EU businesses can claim refunds of Czech VAT by submitting a written application to the tax authority for Prague 1. Refunds are only made on the basis of reciprocity (currently applicable only for Switzerland, Norway and Macedonia).

Other notes

Local reverse charge for selected transactions

The reverse charge mechanism applies to supplies of gold, scrap materials and waste, construction and assembly works and emission rights effected between Czech VAT payers.

As of 1 April 2015, the application of the reverse-charge mechanism has been extended to cereal and technical crops, metals, mobile phones, integrated circuits, tablets, laptops, and videogame consoles. Furthermore, as of 1 September 2015, the mechanism has been applied also to sugar beets. The mechanism shall be applied when the commodities are supplied between two domestic VAT payers and if the total tax base for all of the selected goods supplied exceeds CZK 100,000 (the limit is relevant only for goods subject to the local reverse-

charge mechanism from 2015). According to a proposed amendment, the reverse-charge regime could be applied also to supplies below CZK 100,000 provided that the contracting parties agree on this treatment in writing.

Further changes related to the local reverse charge mechanism came into effect in 2016. The local reverse charge mechanism now applies to supplies of immovable property, unless they are exempt. As of February 2016, the local reverse charge mechanism should also apply to supplies of gas and electricity to a dealer and to supplies of electricity certificates.

Local supplies of goods effected by a person not established in the Czech Republic

According to a proposed amendment, as of May 2016 the reverse charge mechanism should also apply to local supplies of goods effected by a person not established in the Czech Republic to a Czech VAT payer unless the supplier is already registered as a Czech VAT payer.

Bad debt relief

A VAT payer is allowed to claim a VAT refund for uncollectible receivables (bad debts). A VAT refund should be possible for certain receivables after maturity, where the debtor is under bankruptcy proceedings.

Liability for payment of VAT

As the recipient of a taxable supply a Czech VAT payer can be liable for VAT from the received supply if it has not been paid by the supplier.

The tax authority may demand VAT payment if:

- a supplier intentionally failed to pay VAT and the customer knew or should have known of this fact;
- the price for the received taxable supply is clearly and unjustifiably different from an arm's length price;
- consideration for a taxable supply is remitted to a foreign account;
- the supplier has been identified by the tax authority as an unreliable VAT payer;
- the payment is made to a bank account which is not published in the tax authority's register (liability is only applied if the payment exceeds CZK 540,000, including VAT);
- fuel is supplied by a fuel distributor not published as a registered distributor of fuel at the moment of taxable supply.

Customs duties

As the Czech Republic is an EU member state, customs matters are governed by EU law. Customs duties are payable on goods imported from outside the EU. Customs rates depend on the type of goods.

The Czech Republic has an Inward Processing Regime (IPR), which effectively allows a Czech manufacturer to import, process and export goods exempt of customs duty and VAT.

Excise duties

Excise duty is payable on hydrocarbon fuels and lubricants, wine, spirits, beer, and tobacco products. Excise duties are fixed at a set amount per unit for each group of products.

The Czech Act on Excise Duty implements EU rules governing the production of excise goods and their release into free circulation. They must generally be produced in a tax warehouse. Once removed from the tax warehouse, they must be released into free circulation and excise duty must be paid. The regime of the suspension exemption can be applied if excise goods are transported to another EU member state or exported.

Energy taxes

Energy taxes include tax on natural gas and other gases, electricity and solid fuels. Only supplies of such products delivered within the Czech Republic are subject to tax. The rules for energy taxes are harmonised within the EU.

The rates of energy taxes are fixed at a set amount per unit for each group of products.

An exemption from energy tax may be claimed under certain conditions, e.g. if the energy is used in metallurgical or mineralogical processes, the electricity is generated from renewable sources or natural gas and other gases are used for the production of heat for households and heating facilities.



***Pivo /pivo/**

Beer - A fermented bitter-tasting alcoholic beverage

Made of malted grains, water, hops and brewer's yeast. It is the most frequently consumed alcoholic beverage in the Czech Republic. Pilsner beer is very popular thanks to its strong hops flavour.

Financial reporting and audit

The extent of disclosures in Czech accounting legislation is considerably less demanding compared to IFRS. IFRS can/must be used under specific conditions.

Financial reporting

Main features of financial reporting

Czech accounting rules are similar to International Financial Reporting Standards (IFRS), although there are some significant differences. In particular, Czech accounting rules are much less detailed compared to IFRS.

The Act on Accounting serves as the main framework, and detailed guidance is provided in the Decree on Double-Entry Accounting and the Czech Accounting Standards.

Different decrees and standards specify the rules and standards for different types of corporations (accounting units), e.g. companies, sole entrepreneurs, banks, insurance companies and non-profit organisations, as well as municipalities and institutions financed by the state.

All corporations recorded in the Commercial Register are obliged to use double-entry book-keeping. Some specific accounting units that are not recorded in the Commercial Register are permitted to keep simplified accounting records (tax evidence).

All corporations recorded in the Commercial Register are obliged to publish their annual statutory financial statements, annual reports and consolidated financial statements in the

Commercial Register; all financial data about all Czech corporations is thus publicly accessible.

The Act on Accounting defines public interests entities in line with EU legislation; i.e. accounting units whose transferable securities are admitted to trading on a regulated market, credit institutions and insurance companies.

All accounting units and groups are categorised depending on the following criteria: net turnover, balance sheet total and number of employees. In total, there are four accounting unit categories (micro, small, medium and large) and three group categories (small, medium and large).

All accounting records must be in Czech.

All accounting records must be kept and financial statements presented in Czech crowns (CZK).

It is possible to specify a business year-end other than 31 December.

An annual physical count of inventory and fixed assets is required.

The general structure of accounts must be in accordance with the standard chart of accounts. Statutory financial statements consist of a balance sheet, an income statement (minimally classified by nature), a cash flow statement, a statement of changes in equity and notes.

Different categories of accounting units disclose different information in their financial statements (e.g. the cash flow statement and the statement of changes in equity are mandatory for medium and large entities only; there are different requirements for disclosures in the notes, etc.).

The exact layout, structure and headings of the balance sheet, the income statement and the cash-flow statement are set in prescribed templates, and minimum disclosures in notes are prescribed in the decrees. The extent of disclosures in Czech accounting legislation is considerably less demanding compared to IFRS.

A separate annual report must be prepared by all accounting units that are subject to a mandatory statutory audit.

A separate report on payments to governments must be prepared by large entities and public interest entities that are active in extractive industries or in the logging of primary forests. All accounting units with shares or bonds publicly listed in the EU must maintain books and prepare their financial statements in accordance with IFRS, as adopted by the EU.

All other accounting units may choose to maintain books and prepare their financial statements in accordance with IFRS if they are consolidated by a parent or an ultimate parent

company in accordance with IFRS, or if they have to consolidate, and if they prepare both standalone and consolidated financial statements in accordance with IFRS.

The Act on Accounting requires that consolidated financial statements be prepared for an accounting unit that is a controlling entity. Subsidiaries and accounting units over which significant influence is exercised are deemed consolidated accounting units.

The obligation to consolidate applies to medium and large groups. Small groups must consolidate only if they include a public interest entity.

Consolidation is not obligatory where the consolidating entity is part of another consolidating entity that is governed by the law of an EU member state, and where specific prescribed conditions have been met. However, this rule does not exempt from the obligation to publish consolidated financial statements as mentioned above. A Czech corporation using the exemption not to consolidate has to translate and publish the consolidated financials of its parent or ultimate parent.

The above exemption from the duty to prepare consolidated financial statements does not apply to banks, insurers and reinsurers, and publicly listed share or bond issuers.

The Act on Accounting also requires that all corporations for which audit is compulsory (see below) are obliged to prepare an annual report in addition to financial statements. The Act on Accounting and also some other acts specify the disclosure requirements of the annual report. Financial statements are an integral part of the annual report as well.

The Act on Corporations requires that all corporations that are part of a group prepare a report on relations between related parties. This report forms an integral part of the annual report where relevant.

Auditing requirements

Audits are compulsory for:

- large accounting units;
- medium accounting units;
- small accounting units that are joint-stock companies and that, in both the current and previous accounting period, have met at least one of the following criteria:
 - net turnover exceeds CZK 80 million per annum;
 - total assets exceed CZK 40 million;
 - the average number of employees exceeds 50;

- all other small accounting units that meet at least two of the above criteria in both the current and previous accounting period;
- foundations and certain other non-profit organisations.

Audit requirements also apply to annual reports:

- The auditor expresses an opinion on whether the annual report is consistent with the financial statements for the same financial year and whether it was prepared in accordance with legal requirements; or
- the auditor issues only one report which comprises their opinion on both the financial statements and the annual report.

The Act on Auditors defines the responsibility of the Chamber of Auditors, which authorises auditors and sets the standards for audits. Audits are carried out in accordance with the International Standards on Auditing issued by the International Federation of Accountants (IFAC) and relevant guidance (*aplikační doložky*) of the Chamber of Auditors of the Czech Republic. Auditors must be appointed by a corporation's general meeting and its supervisory board is responsible for audit quality supervision. Public interest entities are also defined in the Act on Auditors, which stipulates responsi-

bilities for both public interest entities and their auditors, e.g. audit committees, lead partner rotation, and transparency reports.

Extensive amendments to the Act on Auditors are expected around mid-2016 in relation to the new EU regulation that will require mandatory firm rotation for public interest entities and impose other limitations on audit/non-audit services provided to public interest entities.





***Buchta /buxta/
Stuffed sweet bun**

A type of sweet leavened pastry of Czech origin with a filling (most often poppy-seed, curd-cheese, plum jam but also custard). Each buchta is made separately and placed into a cake tin directly next to another to make them easy to break apart after baking.

Corporate transactions

Corporate transactions have become an important feature of the Czech legal environment, making it possible for entrepreneurs to expand or restructure their business activities in the Czech Republic.

Corporate transactions have become an important feature of the Czech legal environment, making it possible for entrepreneurs to expand or restructure their business activities in the Czech Republic. The process of mergers and acquisitions is primarily regulated by the Civil Code, the Act on Business Corporations, the Act on Takeover Bids, the Act on Transformations of Business Companies and Co-operatives, accounting and tax laws, anti-monopoly regulations, and a number of special regulations applicable to specific sectors, such as banking, insurance and other financial services.

Privatisation

Although it is not currently a hot topic, a number of enterprises in sectors such as electricity and transport may still be subject to potential privatisation by sale to strategic investors. The privatisation process is initiated by government decision. All transactions are subsequently carried out by the relevant ministry, generally through a tender.

Ownership of real estate

The Czech Republic does not place any restrictions on real estate ownership.

Acquisition and disposal of czech legal entities

For foreign individuals and legal entities, no restrictions apply to owning a business or holding shares in companies, and they may acquire and sell up to 100 percent of the share capital of a limited liability or joint-stock company. Likewise, foreign individuals and legal entities can also participate in companies with other legal forms.

The transfer of an ownership interest in a limited liability company must be recorded in the Commercial Register. The shares of certain joint-stock companies are registered with the Central Securities Depository Prague or deposited in escrow at the Central Securities Depository Prague, a bank or other entity entitled to maintain records of investment instruments. In the case of shares traded on the regulated securities market in the Czech Republic or another EU member state, the acquirer is obliged to notify the company (the issuer) and the Czech National Bank if their share of the company's voting rights exceeds a certain level. In addition, if shareholders acquire a minimum of 30 percent of voting rights and actually control the company, they are obliged to bid for the shares of the remaining shareholders.

Purchases of enterprises

An acquisition can also be made by purchasing an enterprise or its parts, with the buyer acquiring the rights, assets and liabilities connected with running the business. The sale and purchase agreement associated with the acquisition must be approved by the general meeting or the shareholders of the company.

Contributions to companies

Another way of securing a share in a business is by making a financial or non-monetary contribution upon which the general meeting of the company must decide on a new share issue. The increase is registered at the Commercial Court. With some exceptions, in cases of non-monetary contributions, an independent valuation of the investment by an independent, generally accepted expert listed in a special register must be submitted.

Transformations of companies

(merger, transfer of assets to a shareholder, demerger, change of legal form and cross-border relocation)

If several entities are controlled by one person, it is possible to consolidate or restructure them. In Czech legislation, mergers come under the category of transformations of businesses,

which also include demergers of companies, transfers of assets to shareholders, any changes in a company's legal form and cross-border relocations. Transformations of businesses are possible even if the companies are in liquidation or insolvency proceedings. Transformations can be undertaken as national or cross-border transactions with legal entities registered in other EU or EEA countries, including European Companies (Societas Europaea). Probably the most frequent form of transformation is the merger by acquisition: one of the companies carries on its activities and the other ceases to exist while its assets and liabilities are transferred to the successor company. Another option is the merger by formation of a new company: all of the participating companies cease to exist, and their assets are transferred to a newly established successor company.

From a financial point of view, carrying forward the tax losses of wound up companies is generally allowed.

- Mergers are carried out on the basis of merger projects, subject to approval by the general meetings.
- The merger date can be determined either retrospectively or prospectively.

- In some cases, the merger procedure can be significantly simplified.
- In the case of mergers of joint-stock companies, it is possible to allow the voluntary buyout of new shares representing a minority share in the merging company, if the successor company owns more than 90 percent of the merging company's voting rights.

Companies with different legal forms can also merge, and mergers may involve more than two entities.

Cross-border mergers are possible; however, a number of special regulations apply.

The transfer of assets to a shareholder is a legal form of company transformation in which a company's assets are transferred to a shareholder owning more than 90 percent of the company's registered capital and also representing more than 90 percent of the company's voting rights.

A company can be demerged (divided) through:

- demerger by formation of new companies;
- demerger by acquisition;
- spin-off connected with new company formation;
- spin-off connected with acquisition;

- a combination of the options mentioned under either 1 or 2 or 3 and 4.

Upon the demerger of a company by the formation of new companies or by acquisition, the company being demerged ceases to exist without liquidation, while in a demerger by spin-off its existence continues.

Czech legislation allows a company to change its legal form solely by changing its internal legal position and structure, but not having to cease to exist.

Under certain conditions stipulated by Czech legislation, a foreign company with its registered office in another EU or EEA country can relocate to the Czech Republic while a Czech company can relocate to another EU or EEA country.

Public bid for purchase or exchange of participating securities issued by a joint-stock company

Should someone (an entity or individual) intend to make an offer to more than 100 shareholders or if the volume of requested securities exceeds one percent of the issue of the regulated market, the offer must be made in the form of a public bid. If a public bid is required by law, the offer must correspond to the value

of the participating securities. If the securities are traded on the regulated market, the bidder must submit an offer and provide evidence to the CNB that consideration for the trade is adequate.

Takeover bids

Voluntary takeover bids

For joint-stock companies traded on the regulated market, investors can make a public offer to the shareholders, if the bid allows them to gain control over the company.

Obligatory takeover bids

An investor acquiring a minimum of 30 percent of the voting rights in a target company traded on the European regulated market and actually gaining control of the company, must offer to buy out the other shareholders within 30 days of the acquisition by, submitting an obligatory takeover bid.

An obligatory takeover bid may be published only after it has been approved by the CNB.

Obligatory takeover bids are also required if a company decides to displace its shares from trading on the European or other foreign

regulated market, or changes the nature of its shares or their transferability.

Right to buy out participation securities (squeeze-out)

A shareholder owning securities representing more than a 90-percent share of the voting rights of a joint-stock company (a major shareholder) is entitled to ask the board of directors to convene a general meeting to decide on the transfer of all the other participating securities owned by minority shareholders, resulting in a squeeze out of minority shareholders. The general meeting of the company approves the squeeze out by paying minority shareholders adequate compensation determined through an expert valuation. Should the shares be traded on the European regulated market, a justification of the compensation and the prior consent of the CNB is required.

In contrast, minority shareholder have the right to sell their shares to the major shareholder as defined above.

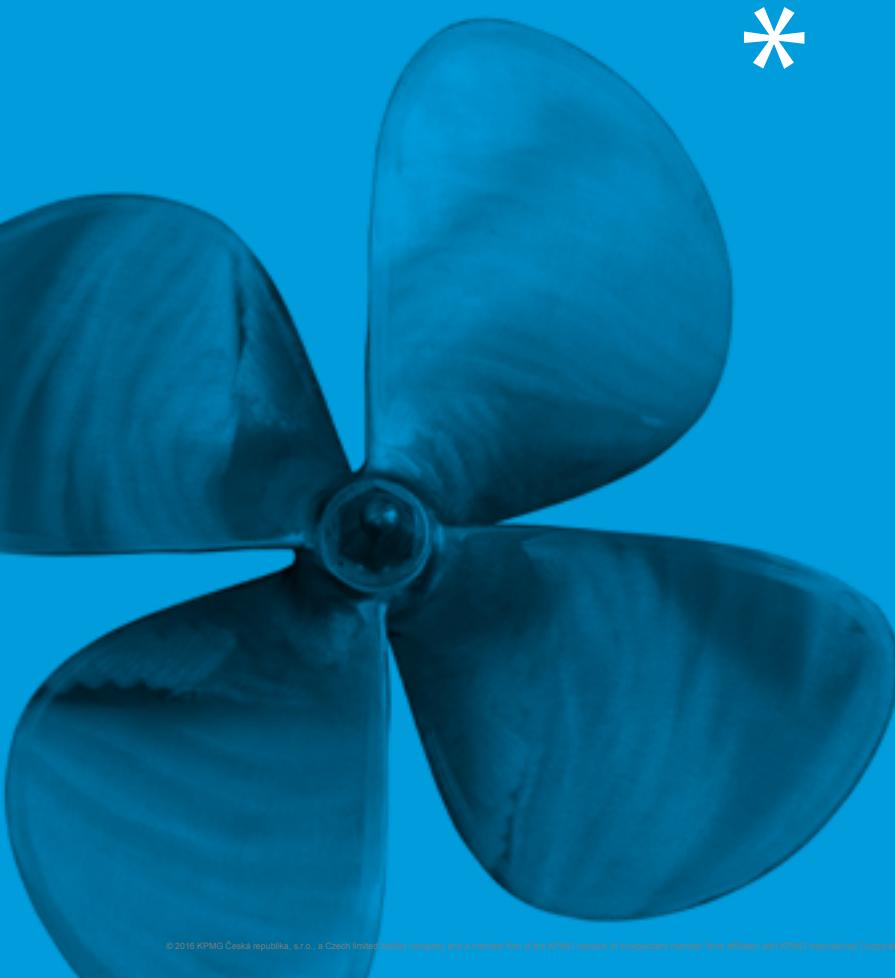
Regulations

With regard to mergers and acquisitions, the interests of minority shareholders are protected as companies are obliged to ensure early notification and, for the majority of transactions, the opinion of an independent expert to determine whether the parameters of the transaction, in particular the price, are fair and reasonable. In the Czech Republic, mergers and acquisitions are also regulated by special legal measures. For example, for a transaction to come into effect in the banking and insurance sector, the appropriate authorities (the CNB and the Ministry of Finance) must give their prior consent.

Mergers and acquisitions also fall within the jurisdiction of the Office for the Protection of Competition. Its permission is required if:

- the aggregate net turnover of the participants in a transaction in the Czech Republic for the prior accounting period exceeded CZK 1.5 billion and at least two of the merging companies each recorded a net turnover of more than CZK 250 million in the Czech Republic for the same period; or
- one or more of the participants in the transaction had a net turnover in the Czech Republic of at least CZK 1.5 billion in the previous accounting period and the worldwide net turnover recorded by the other participant exceeded CZK 1.5 billion for the same period.





***Lodní šroub /lodni: ſroub/
Propeller**

A Czech invention of Mr. Josef Ressel (patented in 1827) that moves ships forward. Its rotation under the water creates a force that pushes backwards a mass of water, allowing the boat to move. Propellers replaced steamboats and are still used today.

How KPMG can help

KPMG in the Czech Republic is the advisor of choice for many businesses who have selected the Czech Republic as an investment location.

We can assist in the following areas

We understand the challenges and pressures faced by those looking to set up business in a new jurisdiction. We can work with you to help you focus on what matters, to avoid pitfalls and unnecessary costs and to ensure your investment projects will start to deliver a measurable return in the shortest possible time frame.

We work with both leading names as well as start-up companies in every sector.

As a result, KPMG in the Czech Republic has become the advisor of choice to many who have selected the Czech Republic as an investment location, providing all the support required to ensure continued business success. Thanks to the KPMG global network of professional firms, we can also work with you in your home country to maximize the potential of your investment in the Czech Republic.

Initial assessment and start-up

A timely, pragmatic and cost effective assessment of the key issues, including the most beneficial corporate and tax structures available, any potential for maximising group taxation benefits on a global basis and available grant assistance. We can also advise on employee benefit issues, e.g. those relating to foreign and Czech state option schemes. We also provide practical business-focused advice and support in dealing with areas such as incorporations and grant application and assessment.

Ongoing business

We offer a broad range of audit, tax, advisory and legal services designed to ensure that investors in the Czech Republic continue to receive timely, proactive and relevant advice and support.

Our services

Audit

- Audits of Czech financial statements
- Audits of financial statements (IFRS, US GAAP, HGB, etc.)
- Audits of financial reports and information
- Audits of prospective financial information
- Review reports
- Reporting on internal control systems
- Sustainability reporting

Petr Škoda

Partner in charge of Audit
T: +420 222 123 548
E: pskoda@kpmg.cz

Tax Services

- Corporate tax
- Indirect tax
- International executive services
- International tax
- Investment incentives and subsidies
- Mergers and acquisitions

- Transfer pricing
- Tax inspections and tax disputes
- Tax services for the financial sector
- Tax outsourcing

Legal Services

- Corporate law
- Transactions and restructuring
- Labour law
- Regulatory issues

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E: rhalicek@kpmg.cz

Management Consulting

- Corporate strategy
- Enterprise architecture
- Finance, capital and profit management
- Programme and project management

- People and change
- EU funds advisory
- Marketing advisory
- IT advisory
- Export advisory
- Customers and sales
- Business intelligence (BI) and data management
- Sports and gaming advisory
- Operations management
- Data and analytics

Petr Bučík

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Risk Consulting

- Accounting advisory services
- Financial risk management
- Internal audit, risk consulting services
- Regional and local authorities and organisations

Romana Benešová

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Deal Advisory

- Corporate finance
- Restructuring
- Transaction services
- Forensic

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Accounting Services and Payroll

- Management reporting
- Financial accounting
- Payroll outsourcing
- Administrative support

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Our priority sectors:

- Automotive
- Banking
- Building, Construction and Real Estate
- Consumer Markets
- Energy
- Food and Drink
- Government and Public Sector
- Healthcare
- Industrial Manufacturing
- Insurance
- Middle Markets
- Retail
- Sports and Gaming
- Telecommunications
- Transportation
- Travel, Leisure and Tourism

Our foreign desks:

- Chinese Desk
- German Desk
- Japanese Desk
- Korean Desk
- Russian Desk

KPMG in the Czech Republic

KPMG has been active in the Czech Republic since 1990, when the first office in Prague was opened. Currently, KPMG Czech Republic has 840 employees and offices in Prague, Brno, České Budějovice and Ostrava. KPMG Czech Republic provides Audit, Tax, Advisory and Legal services. Our 700 professionals include 26 partners, 29 certified auditors, 110 certified accountants and 88 tax advisors. At KPMG Czech Republic, we employ a total of 23 qualified foreign practitioners.

KPMG is a global network of professional firms providing Audit, Tax and Advisory services. We operate in 155 countries and have 155,000 employees working in member firms around the world. The independent member firms of the KPMG network are affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. Each KPMG firm is a legally distinct and separate entity and describes itself as such.

Useful addresses

Czech government offices

Ministry of Finance of the Czech Republic

Letenská 15
118 10 Prague 1
T: +420 257 041 111
www.mfcr.cz

Ministry of Industry and Trade of the Czech Republic

Na Františku 32
110 15 Prague 1
T: +420 224 851 111
www.mpo.cz

Ministry for Regional Development of the Czech Republic

Staroměstské náměstí 6
110 15 Prague 1
T: +420 224 861 111
www.mmr.cz

CzechInvest (Investment and Business Development Agency)

Štěpánská 15
120 00 Prague 2
T: +420 296 342 500
www.czechinvest.org

Czech National Bank (the Central Bank of the Czech Republic)

Na Příkopě 28
115 03 Prague 1
T: +420 224 411 111
www.cnb.cz

Banks active in the Czech Republic

An up-to-date list of banks active in the Czech Republic can be found on the website of the Czech National Bank, at: www.cnb.cz

Business organisations

An up-to-date list of business organisations active in the Czech Republic can be found on the BusinessInfo portal, at: www.businessinfo.cz

Contact us

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