GMS Flash Alert

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Czech Republic - Planned Changes in Taxation of Individuals

The Ministry of Finance of the Czech Republic has published the proposal of amendment to the Income Tax Act which should become effective as of 1 January 2019.[1] The principles of taxation of individuals are to change fundamentally.

Highlights of the changes we discuss in this newsletter are:

- Abolition of the 15-percent flat rate and the 7-percent solidarity tax.
- Elimination of the current calculation of personal income tax on super-gross salary.
- The introduction of progressive tax rates of 19 percent for income of up to CZK 1.5 million and 24 percent (may be 23 percent) for income above this amount. [CZK 1 = USD 0.0485 | CZK 1 = EUR 0.04 | CZK 1 = GBP 0.035]

WHY THIS MATTERS

The total effective taxation on employees should remain the same. However, employers should be prepared for the new mechanism of calculating wage tax advances.

Similarly, self-employed individuals will also be subject to progressive tax rates; however, they will now be entitled to deduct 75 percent of their social and health security contributions. Their effective tax rate should not therefore change significantly.

A potentially higher effective tax burden will be applied on capital gain and rental income.

Abolition of Flat Rate and Solidarity Tax, Progressive Rates Introduced

The proposed changes include abolition of the 15-percent flat rate and the 7-percent solidarity tax.[2] The flat rate tax under current law, has been applied to all types of personal income (i.e., income from dependent activities, income from self-employment, rental income, dividend income, capital gain income, etc.).

The 7-percent solidarity tax has applied to the sum of employment income and self-employment income exceeding the annual cap for social security contributions (CZK 1,438,992 in 2018), but has not applied to other types of income.

Effective 1 January 2019, these two taxes are expected to be eliminated.

However, the government is proposing progressive income taxation from that date, with a 19-percent rate applying to income up to CZK 1.5 million and 24 percent (may be 23 percent) for income above CZK 1.5 million.

Personal Income Tax on Super-Gross Salary

Super-gross salary is defined as gross salary increased by 34 percent which represents either actual or hypothetical employer's portion of social security contributions). Since 2008 the 15-percent flat income tax rate has applied to super-gross salary. Now, under the proposed amendment, the current method for calculating personal income tax on super-gross salary will be abolished; instead it will be replaced with the application of progressive tax rates.

Additional Details

The proposed changes should not have a significant impact on the effective taxation of employees: the effective taxation on employment income up to CZK 1.5 million will be slightly lower, by approximately 1.1 percent.

However, taxation of other types of income, mainly rental income and capital gain income will be subject to the higher rates – i.e., 19 percent or 24 percent (or 23 percent) compared with the current 15-percent rate (no solidarity tax applies on these types of income currently).

The new separate tax base is introduced especially for some types of income from abroad, e.g., dividend and interest income, which will be subject to a final 15-percent tax to correspond with the continuing 15-percent withholding tax on domestic dividends and interest.

KPMG NOTE

What we have described above is based on the proposed draft which has yet to be submitted to Parliament. The wording of the proposed amendment of the Income Tax Act may change during the legislative process. Nonetheless, it is expected that the amendments to the Income Tax Act will be effective as of 1 January 2019.

FOOTNOTES:

1 See : (In Czech) *Návrh zákona, kterým se mění některé zákony v oblasti daní od roku 2019* – at: https://apps.odok.cz/veklep-detail?pid=KORNAVKGT7MQ .

2 For further details on the taxation of income, see *Taxation of International Executives: Czech Republic*, a publication of KPMG International.

Contact us

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