GMS Flash Alert

2020-010 | January 15, 2020

Czech Republic - Court Confirms Expat Social Security Income Tax Base

The Supreme Administrative Court decided a case against the Appellate financial directorate of the Czech Republic involving a standard employment structure in which an employee assigned from Japan to work in the Czech Republic was paid partly by his Czech (economic) employer, and partly by his formal/legal employer in Japan.[1]

The Supreme Administrative Court decided that since the employee only performs one job under an employment contract with a single formal/legal employer, the administrative dividing of the costs between the two employers sharing the cost is not relevant in calculating the employee's income tax base.

WHY THIS MATTERS

The remuneration of expatriates who are covered under the social security laws in the countries of their formal/legal employers is increased by "fictitious" premiums, i.e., the social security and health insurance premiums that they would have paid had they been employed in the Czech Republic, when calculating the employee's income tax base. Employers of these expatriates need to be aware of this obligation and calculate the employee's income tax base correctly.

Further Details

The employee from Japan was not covered by Czech social security and remained covered by health insurance and social security in Japan, under Japanese social security law. In determining the employee's income tax base, the employers increased his remuneration by "fictitious" premiums, i.e., the social security and health insurance premiums that he would have paid had he been employed in the Czech Republic. The social security premium was only calculated on one maximum assessment base.

The Czech tax authority first accepted this approach but later, in the course of the employee's assignment, started to challenge it. The tax authority asserted that the money paid from the Czech Republic and Japanese employers constituted two separate incomes from employment and should be increased by the fictitious premiums on two separate bases. This proposed treatment would have resulted in applying a separate maximum assessment base to each employer's calculation. The case was brought before the Supreme Administrative Court.

Referring to an explanatory report to the law, the Supreme Administrative Court confirmed that income has to be increased by statutory insurance premiums in the same manner as if the taxpayer had been covered by Czech social insurance legislation. However, the employee only performed work under one employment contract concluded with a single formal/legal employer, and the manner of dividing the costs between that employer and the economic one was not relevant for calculating the employee's income tax base.

The court also pointed out that the tax authority changed its approach without a sufficient explanation, after a period of not challenging the taxpayer's approach.

FOOTNOTE:

1 Decision (in Czech) of the Supreme Administrative Court no. 4 Afs 164/2019 – 63 (27 September 2019).

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Contact us

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